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No. 98-585

In The

Supreme Court of the United States

October Term, 1998

ROBERT D. KRUMME, *et al.*,

Petitioners,

vs.

WESTPOINT STEVENS INC., formerly known as WEST POINT-PEPPERELL, INC., *et al.*,

Respondents.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Second Circuit

RESPONDENTS' BRIEF IN OPPOSITION

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QUESTIONS PRESENTED

1. Whether Petitioners, who participated in a non-ERISA-qualified deferred compensation plan that incorporated by reference the discount rate contained in an ERISA-qualified pension plan, may collaterally challenge the pension plan administrators' action to change the pension plan's discount rate, where Petitioners brought no claims as participants or beneficiaries of the pension plan and failed to avail themselves of the pension plan's administrative review procedures?

2. Whether nine of the Petitioners, who released their claims under a deferred compensation agreement, should be permitted to argue that the discount rate applicable to a change in control amendment to the deferred compensation agreement was improperly changed, after the district court found as a matter of fact that their releases were valid and should not be rescinded?

3. Whether the written record of a pension plan committee's decision to change the plan's discount factor upon the advice of the plan's independent actuary constitutes a document or instrument governing the plan, where the pension plan expressly provides that "the records of the Committee shall be conclusive and binding upon the Company, Participants, and all persons having any interest under the Plan"?

RULE 29.6 STATEMENT

Respondent WestPoint Stevens Inc., formerly known as West Point-Pepperell, Inc., is a Delaware corporation that has publicly traded shares. It has no parent corporation. WestPoint Stevens Inc. owns 100% of the equity of each of its subsidiaries.

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Respondents WestPoint Stevens Inc. ("WestPoint"), C. Powers Dorsett and D. Michael Roark respectfully submit this brief in opposition to the Petition filed by Robert D. Krumme, *et al.* ("Petitioners") for a writ of certiorari to the United States Court of Appeals for the Second Circuit.[1]

OPINIONS BELOW

The opinion of the Court of Appeals (P. App. 1a-37a) is reported at 143 F.3d 71 (2d Cir. 1998). Relevant opinions of the District Court are reported at 1996 WL 2004 (S.D.N.Y. Jan. 3, 1996) (R. App. 1a-14a), 933 F. Supp. 261 (S.D.N.Y. 1996) (R. App. 15a-35a), and 954 F. Supp. 682 (S.D.N.Y. 1997), as amended in an unpublished opinion which appears at R. App. 36a-64a.

STATUTES INVOLVED

In addition to the statutory provisions cited by Petitioners, the following statutes are involved:

29 U.S.C. § 1051(2) provides:

> § 1051. **Coverage**
>
> This part shall apply to any employee benefit plan described in section 1003(a) of this title (and not exempted under section 1003(b) of this title) other than — . . .

---

1. Petitioners' Petition for a Writ of Certiorari will be cited herein as "Pet." The Appendix to the Petition for a Writ of Certiorari will be cited as "P. App." Portions of the record below cited herein, if not appended to the Petition for Certiorari, are annexed in an Appendix hereto, which is cited as "R. App." Emphasis in passages quoted herein is ours unless otherwise indicated.

> (2) a plan which is unfunded and is maintained by an employer primarily for the purpose of providing deferred compensation for a select group of management or highly compensated employees;

29 U.S.C. § 1101(a)(1) provides:

> § 1101. **Coverage**
>
> (a) This part shall apply to any employee benefit plan described in section 1003(a) of this title (and not exempted under section 1003(b) of this title), other than —
>
> (1) a plan which is unfunded and is maintained by an employer primarily for the purpose of providing deferred compensation for a select group of management or highly compensated employees; or

STATEMENT OF THE CASE

Respondents herein incorporate by reference the Background discussion in the Second Circuit's May 1, 1998 opinion (P. App. 4a-25a). Respondents also incorporate by reference the findings of fact from the District Court's May 13, 1996 opinion denying the *Allen* plaintiffs' request to rescind their releases (R. App. 15a-35a) and the District Court's February 10, 1997 opinion denying the *Allen* plaintiffs' misrepresentation claims (R. App. 36a-64a).

This case arises from WestPoint's efforts in 1989 to correct an outdated discount rate mistakenly included in a deferred compensation plan (the "EPI Program") maintained for senior executives of its wholly-owned subsidiary, Cluett Peabody & Co. ("Cluett"). P. App. 8a-9a.

In 1988, participants in various benefit plans of WestPoint and its subsidiaries were offered "Change in Control" amendments that would permit the present value of their future benefits to be paid in a lump sum in the event the company was taken over. P. App. 5a. The Change in Control amendment for the EPI Program (the "EPI Amendment") was executed by participating Cluett executives ("EPI participants") in late 1988. P. App. 8a.

To determine the EPI participants' lump sums, it was intended that the EPI Amendment incorporate the floating, Pension Benefit Guaranty Corporation ("PBGC")-based discount rate contained in WestPoint's Employee Retirement Plan and referenced in all the other Change in Control amendments to WestPoint's employee benefit plans. R. App. 15a-24a, 31a n.6, 53a. By mistake, however, WestPoint incorporated by reference the discount rate contained in *Cluett's* Employee Retirement Plan (the "Cluett Plan") — an outdated, below-market, fixed rate of 5%. P. App. 8a-9a. At relevant times, the PBGC-based discount rate was approximately 9.3%, or nearly twice the rate in the Cluett Plan. P. App. 9a; R. App. 25a-26a, 30a-32a, 60a-62a. (The lower the discount rate, the larger the resulting lump sum payout to executives.)

In November 1988, Farley, Inc. launched a hostile bid for WestPoint. During the takeover fight, WestPoint discovered the error in the EPI Amendment. WestPoint reviewed the Cluett Employee Retirement Plan, the source of the outdated discount rate, and found that the discount factor in the Cluett Plan could be changed by the Committee appointed to administer the Cluett Plan (the "Committee"), on advice of the plan actuary. Accordingly, upon the recommendation of the plan actuary, the Committee changed the Cluett Plan's discount rate to the PBGC-based formula on February 16, 1989. That change was duly recorded in the minutes of the Committee. P. App. 9a-10a; R. App. 25a, 72a-73a, 74a.

At the time, Petitioner Robert D. Krumme ("Krumme"), a former General Counsel of Cluett, protested that he and others had relied on the 5% rate in executing the EPI Amendment. Consequently, WestPoint notified all the EPI participants of the 9.3% discount rate and offered them the opportunity: (i) to accept the new rate and release WestPoint, or (ii) to revoke their EPI Amendments and return to the original stream of future payments provided under the EPI Program. P. App. 11a; R. App. 75a-76a. Most EPI participants executed Election Forms in which they accepted the 9.3% discount rate and released WestPoint from all further obligations under the EPI program. Krumme, however, sued WestPoint for breach of contract on March 24, 1989 in the United States District Court for the Southern District of New York. *Krumme v. WestPoint-Pepperell, Inc.*, 89 Civ. 3841 (S.D.N.Y.).

A Change in Control occurred on April 5, 1989. R. App. 2a, 14a. The EPI participants who had signed releases were paid lump sums discounted at 9.3% upon the Change in Control. In June 1990, nine EPI participants who had signed releases sued WestPoint, and three of its executives individually, for breach of contract, breach of fiduciary duty, fraud, mutual or unilateral mistake, and failure to pay wages. *Allen v. West Point-Pepperell, Inc.*, 90 Civ. 3841 (S.D.N.Y.) ("*Allen*"). Krumme had recruited all the *Allen* plaintiffs to sue WestPoint before the end of September 1989, and had entered into contingent-fee contracts to represent each of them. P. App. 13a.

A. The District Court Decisions

In November 1995, the District Court granted partial summary judgment to the *Allen* plaintiffs as to the applicable discount rate, and later applied that ruling to Krumme. The District Judge concluded that the Committee's attempt to change the discount rate in the Cluett Plan was ineffective under

ERISA and, for purposes of the EPI Amendment, the Cluett Plan contained a 5% discount rate at all relevant times. P. App. 79a. The District Court stated that, because the Cluett Plan set forth a procedure under which the power to amend was reserved to the Board of Directors, the Committee had no authority under ERISA to change the Cluett Plan's terms. P. App. 71a. The District Judge recognized that her ruling "arguably render[ed] meaningless the Plan's grant of authority to the Cluett Committee to adopt actuarial factors from time to time." P. App. 72a.

Krumme, the *Allen* plaintiffs and WestPoint agreed to try four issues to the Court: (i) the date on which a Change in Control occurred (tried in December 1995); (ii) whether the *Allen* plaintiffs could rescind their releases based on mutual mistake (tried in January 1996); (iii) whether the EPI Amendment required WestPoint to pay the attorneys' fees and costs incurred by Krumme or the *Allen* plaintiffs; and (iv) the *Allen* plaintiffs' claims for damages based on misrepresentation (tried on papers in the Fall of 1996). P. App. 17a.

After a bench trial on Change in Control, the District Court found that the Change in Control occurred on April 5, 1989. R. App. 2a, 14a. No party appealed that decision.

After a bench trial on rescission and attorneys' fees, the District Court declined to rescind the releases executed by the nine *Allen* plaintiffs. The District Court found that the change in the discount rate was "a good-faith effort to correct [a] drafting mistake" (R. App. 31a), and further found that rescinding the releases "would create an entirely unfair result" by forcing WestPoint to pay the *Allen* plaintiffs "nearly twice the market-based present value of their EPI benefits." R. App. 31a. Such an outcome "would undermine the WestPoint Board's understandable desire to harmonize the payout methodologies

used in its various benefit plans," the District Judge observed. Moreover, the District Court found, rescission would give the *Allen* plaintiffs "an undeserved and unintended windfall." R. App. 31a.

After a bench trial on the *Allen* plaintiffs' claims for damages based on alleged misrepresentations concerning the discount rate, the District Court found that WestPoint and the individual defendants had not made any false representations. R. App. 52a-53a. The District Court found "no concrete possibility" that the change in the discount rate resulted from a purported conflict of interest on the part of WestPoint executives. R. App. 55a. The District Court concluded that the *Allen* plaintiffs had produced "no evidence that casts doubt on the veracity" of testimony that the defendant WestPoint executives did not expect to benefit personally from changing the discount rate. R. App. 55a. Based on the *Allen* plaintiffs' failure of proof, the District Court found WestPoint and the individual defendants not liable for fraudulent omission, constructive fraud or misrepresentation. R. App. 64a.

In both *Krumme* and *Allen*, the District Court concluded that Petitioners could recover costs and attorneys' fees from WestPoint under the EPI Amendment.[2] However, the District

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2. The EPI Amendment contains a fee-shifting clause which provides that, "[i]f at any time upon or after a Change of Control there should arise any dispute as to the validity, interpretation or application of any term or condition of this Agreement," WestPoint would pay the EPI participant's reasonable attorneys' fees and expenses "regardless of whether the Executive is the prevailing party." R. App. 70a § 16. Among other things, WestPoint contended below that the instant dispute did not arise "upon or after a Change of Control" because the discount rate was changed on February 16, 1989, the *Allen* plaintiffs released their claims in late February 1989, Krumme sued on March 23, 1989, and a Change in Control did not occur until April 5, 1989.

Court deferred determination of the costs and attorneys' fees payable to Krumme and the *Allen* plaintiffs until after an appeal.

B. The Decision of the Second Circuit

WestPoint appealed from the *Krumme* and *Allen* judgments, among other things challenging the District Court's ruling that the Committee's action to change the discount rate from 5% was ineffective and the District Court's decision to shift attorneys' fees. The *Allen* plaintiffs cross-appealed, seeking reversal of the District Court's rulings on rescission and misrepresentation. The *Allen* and *Krumme* cases were consolidated for appeal in the Second Circuit.

On appeal, WestPoint argued (among other things) that (i) the Committee was empowered to change the discount rate by the express terms of the Cluett Plan; (ii) the discount rate could be changed without an amendment to the Plan; and (iii) the plaintiffs failed to avail themselves of the Cluett Plan's administrative remedies and could not collaterally challenge the Committee's action. In opposition, Krumme and the *Allen* plaintiffs argued (among other things) that the Committee had no authority to change the discount rate, which (they asserted) under Revenue Ruling 79-90 could only be changed by Board amendment to the Cluett Plan.

The Court of Appeals ruled that the Cluett Committee effectively adopted the PBGC-based discount rate; that the EPI Amendment incorporated that rate; and that the executives' lump sums were properly calculated using a 9.3% discount factor. P. App. 24a. The Second Circuit held that the Cluett Plan expressly permitted the Committee to adopt a new discount rate without a plan amendment. P. App. 30a. The Court of Appeals observed that § 9.6 of the Cluett Plan made the Committee's written records "conclusive and binding" on the

Cluett Plan sponsor, the plan participants, and "all other persons having any interest under the Plan." P. App. 31a. Thus, the Committee's minutes evidencing adoption of the PBGC-based rate were a "written instrument" under which the Plan was established or operated, and the resulting 9.3% discount rate was "contained in" the Cluett Plan. *Id.*

Because the District Court had not yet set the amount of fees and costs, the Court of Appeals declined to review the lower court's ruling that Petitioners were nonetheless entitled to recover their attorneys' fees under the EPI Amendment. A proceeding to determine attorneys' fees is expected to commence before a Magistrate Judge. Respondents respectfully suggest that, were it not for the District Court's fee-shifting ruling, this certiorari petition would never have been filed. The instant petition, in short, is an example of the attorneys' fee tail wagging the substantive dog.

SUMMARY OF ARGUMENT

There is no basis for granting a writ of certiorari in this case.

First, this case involves an idiosyncratic pension plan provision, as it was applied after being incorporated by reference into a change-in-control amendment to a non-qualified deferred compensation plan. Control of WestPoint changed more than nine years ago. The dispute thus cannot recur, and has no significance to the public at large.

Second, the petition for certiorari should be denied because Petitioners failed to avail themselves of the administrative remedies available under the Cluett Plan, and are thereby barred from collaterally attacking the Committee's action through a lawsuit.

Third, Petitioners misstate the law when they argue that the Committee's action "violate[d]" 26 U.S.C. § 401(a)(25) and Revenue Ruling 79-90. *See* Petitioners' Questions Presented, Question 1. Those provisions are not legal mandates, but rather are voluntary standards that must be met in order to obtain certain tax benefits. Here, the administrative and regulatory agencies charged with enforcing tax-qualification requirements have not taken any action against WestPoint or the Cluett Plan during the 9½ years since the Committee adopted the PBGC-based discount rate. Further, the PBGC-based discount rate complies with the requirements of Revenue Ruling 79-90.

Fourth, the Second Circuit's decision in no way conflicts with ERISA or with this Court's precedent. The *Krumme* and *Allen* cases did *not* concern pension benefits. Rather, the parties disputed the discount rate applicable to a change-in-control amendment for a "top-hat," non-ERISA-qualified, deferred compensation plan offered only to high-level executives. The EPI Amendment was not subject to ERISA's accrued benefit rules and Petitioners' "accrued" benefits under the Cluett Plan were never affected.

Fifth, there is no conflict among the Circuits because the Second Circuit's decision is fully in accord with the Third and Seventh Circuit opinions cited by Petitioners.

Finally, the writ should be denied because the Second Circuit correctly analyzed and applied the disputed provisions of the Cluett Plan and the EPI Amendment. The Committee was expressly charged with the power to change the discount rate, and was not required to amend the Cluett Plan in order to do so. The rate adjustment was duly recorded in the Committee's minutes which, under the terms of the Cluett Plan, constituted an instrument or document governing that Plan.

REASONS FOR DENYING THE WRIT

I.
THIS CASE INVOLVES AN IDIOSYNCRATIC PLAN PROVISION, AND THE UNDERLYING DISPUTES CANNOT RECUR

The present case does not merit review by this Court because the parties' dispute is fact-specific and lacks broader significance.

First, Petitioners ask this Court to determine whether the Committee validly changed the discount rate in the Cluett Plan. But, as this Court has previously noted, whether a plan sponsor has complied with procedures for changing a plan "depend[s] on a fact-intensive inquiry." *Curtiss-Wright Corp. v. Schoonejongen*, 514 U.S. 73, 85 (1995) (remanding similar question on that ground). A petition raising what is "primarily a question of fact . . . does not merit Court review." *National Labor Relations Board v. Hendricks County Rural Elec. Membership Corp.*, 454 U.S. 170, 177 n.8 (1981) (finding that certiorari was improvidently granted when the main issue was whether the Court of Appeals was correct in determining that a person was not the functional equivalent of a personnel department employee, thereby making the National Labor Relations Act applicable).

Second, the only persons who might be affected by the Second Circuit's decision are former executives of Cluett who participated in the EPI Program and executed the EPI Amendment.[3] All the executives except Krumme either released

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3. As the District Court found, the Cluett Plan's discount rate was used only to calculate *de minimis* lump sum distributions under $3,500. R. App. 21a & n.3. A ruling by this Court is therefore unlikely to have a significant effect on Cluett Plan participants. Further, the record does not reveal any challenge to the discount rate by a Cluett Plan participant *qua* participant.

their claims in 1989 or declined to sue. In particular, the nine *Allen* Petitioners released their claims under the EPI Amendment and accepted WestPoint's payout at the 9.3% PBGC-based rate. The District Court held two trials on whether those releases resulted from mistake or misrepresentation, and in each case found that they did not. The District Court's factual findings in that regard must be upheld unless clearly erroneous.[4] Because the District Judge made her factual rulings while under the impression that the correct discount rate was 5%, *see* R. App. 18a-19a, 37a, reversal of the Second Circuit's contrary determination should not affect the releases' validity.

Thus, Krumme is the only person with a real, non-speculative interest in obtaining reversal of the Second Circuit's decision. The Supreme Court "does [not] sit for the benefit of the particular litigants," and certiorari is inappropriate where the "question [is] of importance merely to the litigants and [does] not present an issue of immediate public significance." *Rice v. Sioux City Memorial Park Cemetery*, 349 U.S. 70, 74, 79 (1955) (internal citation omitted); *accord Layne & Bowler Corp. v. Western Well Works, Inc.*, 261 U.S. 387, 393 (1923) (when a case involves no issues that are "importan[t] to the public, as distinguished from . . . the parties," certiorari should be denied). Whether Krumme should recover the difference between his lump sum payment discounted at 9.3% and a payment discounted at 5% is not a question that warrants the attention of this Court.

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4. *Amadeo v. Zant*, 486 U.S. 214, 223 (1988) ("It is well settled . . . that a federal appellate court may set aside a trial court's findings of facts only if they are 'clearly erroneous.' ") (citing Fed. R. Civ. P. 52(a)); *accord Anderson v. Bessemer City*, 470 U.S. 564, 573 (1985) (describing "clearly erroneous" standard generally).

II.

PETITIONERS FAILED TO AVAIL THEMSELVES OF ADMINISTRATIVE REMEDIES UNDER THE CLUETT PLAN

Certiorari should not be granted because Petitioners failed to avail themselves of the administrative remedies under the Cluett Plan. Although the Cluett Plan provides a two-step appeal procedure for benefit determinations, *see* R. App. 66a § 9.8, Petitioners made no use of it. Instead of challenging the Committee's action as Cluett Plan participants, they mounted a collateral attack on the discount rate change through two federal lawsuits.

Every Circuit to consider the issue has held that failure to exhaust a plan's administrative remedies bars a lawsuit for additional benefits under ERISA.[5] That rule, along with Petitioners' inaction at the Plan level, makes this matter unsuitable for Supreme Court review.

III.

THE INTERNAL REVENUE CODE AND REVENUE RULING 79-90 WERE NOT VIOLATED

Petitioners' argument that the Committee's adoption of the PBGC-based rate violated 26 U.S.C. § 401(a)(25) and Revenue Ruling 79-90 mischaracterizes the law. Section 401(a)(25) and

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5. *See, e.g., Hall v. National Gypsum Co.*, 105 F.3d 225, 231 (5th Cir. 1997); *Wilczynski v. Lumbermens Mut. Cas. Co.*, 93 F.3d 397, 401-02 (7th Cir. 1996); *Hickey v. Digital Equip. Corp.*, 43 F.3d 941, 945 (4th Cir. 1995); *Communications Workers v. AT&T*, 40 F.3d 426, 431-32 (D.C. Cir. 1994); *Kennedy v. Empire Blue Cross & Blue Shield*, 989 F.2d 588, 594 (2d Cir. 1993); *Alfarone v. Bernie Wolff Constr. Corp.*, 788 F.2d 76, 79 (2d Cir. 1986); *Amato v. Bernard*, 618 F.2d 559, 567 (9th Cir. 1980).

the Revenue Ruling impose no legal mandate. Rather, they simply set voluntary conditions for qualification that, if not met, could potentially result in adverse tax consequences. *See* 29 U.S.C. § 1202 (coordinating various agencies' efforts with respect to application of tax regulations to pension plans).

Failure to comply with Revenue Ruling 79-90 and 26 U.S.C. § 401(a)(25) would thus affect only the Cluett Plan's tax-exempt status. Actuarial assumptions adopted in ways other than those specified in the tax law would still remain valid and effective among the parties.[6] As a result, a decision by this Court construing the tax-qualification requirements for pension plans would not alter the 9.3% discount rate.

Notably, those agencies charged with enforcing the provisions cited by Petitioners have expressed no concern over the Committee's adjustment of the discount rate. The record reveals no proceeding against the Committee, the Cluett Pension

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6. *See Reklau v. Merchants Nat'l Corp.*, 808 F.2d 628, 631 (7th Cir. 1986) (provisions of Internal Revenue Code § 401 "relate solely to the criteria for tax qualification under the Internal Revenue Code" and are not imposed on pension plans by ERISA) (citation omitted); *accord Huber v. Casablanca Indus., Inc.*, 916 F.2d 85, 106 (3d Cir. 1990) (amendments to plan were valid even though employer's annual reports to Department of Labor indicated that no amendments had been adopted; "[w]hatever the consequences that may flow in other forums from the Trustees' failure to have reported those amendments, that failure cannot be found to invalidate the plan amendments"), *cert. dismissed*, 506 U.S. 1088 (1993), *overruled in part on other grounds by Milwaukee Brewery Workers Pens. Plan v. Jos. Schlitz Brewing Co.*, 513 U.S. 414 (1995); *Chemtech Inds., Inc. v. Goldman Financial Group Inc.*, 156 F.R.D. 181, 184 (E.D. Mo. 1994) (in dismissing ERISA claim against defendants, court noted that § 401 of the Internal Revenue Code relied upon by plaintiffs "ha[s] not been imposed on employee benefit plans by the substantive terms of ERISA"); *Cooke v. Lynn Sand & Stone Co.*, 673 F. Supp. 14, 21 n.8, 22-23 (D. Mass. 1986) (Revenue Ruling 79-90 "was incorporated into the Internal Revenue Code, but not ERISA").

Plan, or WestPoint by the Internal Revenue Service, the Department of Labor, the Pension Benefit Guaranty Corporation, or any other organization charged with responsibility for such matters during the 9½ years since the PBGC-based discount rate was adopted.

In any event, Revenue Ruling 79-90 itself states that it can be satisfied by "a variable standard which provides for self-adjusting changes which are independent of employer discretion," for example, a provision "specifying that the interest rate will be a designated percentage of the prime interest rate of a specified bank or banks at the time of the benefit determination." The floating, self-adjusting, PBGC-based discount rate adopted by the Committee is precisely that type of standard.

IV.

THE COURT OF APPEALS' DECISION DOES NOT CONFLICT WITH ERISA OR WITH THIS COURT'S PRECEDENT

The Second Circuit's decision does not conflict with this Court's precedent, nor does it "make a shambles" of ERISA's scheme for protecting accrued pension benefits (Pet. 12). In fact, the decision below does not affect accrued pension benefits at all.

A. The Second Circuit's Opinion Does Not Conflict With 29 U.S.C. § 1054(g)

Under 29 U.S.C. § 1054(g), "[t]he accrued benefit of a participant plan may not be decreased by an amendment of the plan." Although relied upon by Petitioners, that section of ERISA does not apply to this case.

First, Petitioners did not sue for their pension benefits under the Cluett Plan. Rather, they attacked the Committee's action collaterally in a lawsuit to obtain a higher payout under the EPI Amendment, a *non*-ERISA-qualified "top-hat" deferred compensation plan. A "top-hat" plan is

> a plan which is unfunded and is maintained by an employer primarily for the purpose of providing deferred compensation for a select group of management or highly compensated employees.

29 U.S.C. §§ 1051(2), 1101(a)(1). The EPI Program was a top-hat plan: its future stream of payments was "Deferred Compensation"; it was unfunded; and the EPI participants were all senior executives of Cluett. R. App. 17a; 68a.

ERISA exempts top-hat plans from most of the requirements ordinarily applicable to employee benefit plans, including the prohibition on cutbacks in accrued benefits in 29 U.S.C. § 1054(g) and the requirements concerning authority to amend the plan in 29 U.S.C. § 1102(b)(3) — the two provisions that Petitioners assert were violated by the Committee's action. *See* 29 U.S.C. §§ 1101(a)(1), 1051(2).

Second, there were no "accrued" benefits under the EPI Amendment to be reduced. No lump-sum payout was due under the EPI Amendment until "the occurrence of a Change in Control." R. App. 69a-70a, ¶4A(2). The Committee changed the discount rate on February 16, 1989. P. App. 9a-10a. The District Court found as a fact that the Change in Control did not occur until April 5, 1989, and no party appealed that decision. R. App. 2a. Thus, no right to a lump sum at a particular discount rate had accrued under the EPI Amendment at the time the discount rate was changed.[7]

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7. EPI participants who did not wish to take a lump sum discounted at 9.3% could retain the full, future stream of payments previously available under the EPI Program, thus losing nothing. R. App. 75a-76a.

Third, the discount rate was *not* changed by amendment. Instead, it was changed by a Committee action that, rather than amending the Plan, exercised an existing grant of authority to adopt a new discount factor *without* amendment. P. App. 30a-31a. The prohibition of 29 U.S.C. § 1054(g), in contrast, "is specifically limited to *actual amendments.*" *Stewart v. National Shopmen Pension Fund*, 730 F.2d 1552, 1563 (D.C. Cir. 1984) (emphasis in original), *cert. denied*, 469 U.S. 834 (1984). Applying the provision to actions other than plan amendments "would require [courts] to ignore" the statute's plain language. *Id.*[8]

Fourth, the administrators of the Cluett Plan did not implement the changed discount rate so as to reduce anyone's accrued pension benefits. Rather, they used a "split" rate, applying the 5% factor to benefits accrued before February 16, 1989 and the PBGC-based rate to benefits accrued afterward. R. App. 77a-78a. The "split" discount rate, however, applied *only* to the Cluett Plan, under which some benefits had vested before February 16, 1989 — it did *not* apply to the EPI Amendment, since EPI participants were not entitled to a lump sum unless and until a Change in Control had occurred.

B. The Second Circuit's Opinion Does Not Conflict With *Curtiss-Wright*

There is no conflict between the Second Circuit's opinion and this Court's statements in *Curtiss-Wright Corporation v. Schoonejongen*, 514 U.S. 73 (1995), to the effect that employee benefit plans must be established and maintained pursuant to a written instrument. The Cluett Plan *was* a written document. It

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8. *Accord Oster v. Barco of California Employees' Retirement Plan*, 869 F.2d 1215, 1220-21 (9th Cir. 1988); *Dooley v. American Airlines Inc.*, 797 F.2d 1447, 1450-52 (7th Cir. 1986), *cert. denied*, 479 U.S. 1032, 1087 (1987); *IAM Ownership Investment Trust Fund v. Eastern Air Lines, Inc.*, 639 F. Supp. 1027, 1034 (D. Del. 1986).

also incorporated by reference *other* written documents — namely, the Committee's decisions and records — and provided in § 9.6 that those decisions and records "shall be conclusive and binding" upon the plan sponsor, participants, and any other person having an interest under the Cluett Plan. R. App. 65a-66a § 9.6. Together, the Cluett Plan, the Committee minutes and other governing documents constituted the "written instrument" under which the Cluett Plan was "established and maintained." *See* 29 U.S.C. § 1102(a)(1).

Petitioners cannot seriously contend that an ERISA plan must be a *single* document. *Curtiss-Wright* indicates the contrary. The *Curtiss-Wright* Court used the plural form when explaining that the purpose of ERISA's written document requirement is to allow an employee "*on examining the plan documents*, [to] determine exactly what his rights and obligations are under the plan." *Curtiss-Wright*, 514 U.S. at 83 (quoting ERISA legislative history) (emphasis in quoted material). The Court in *Curtiss-Wright* went on to describe Summary Plan Descriptions, plan amendment summaries, and other "governing plan *documents*" that must be made available to plan participants. *Accord* 29 U.S.C. § 1104(a)(1)(D) (requiring that fiduciaries generally act "in accordance with the *documents* and *instruments* governing the plan"). Lower federal courts agree that ERISA plans may include more than one document.[9]

9. *See, e.g., Rinard v. Eastern Co.*, 978 F.2d 265, 268 n.2 (6th Cir. 1992) (ERISA does not require that a plan be a single document), *cert. denied*, 507 U.S. 1029 (1993); *Bright v. SKW Alloys Group Ins. Plan*, 823 F. Supp. 428, 431 (W.D. Ky. 1993) ("ERISA does not require the terms of an ERISA plan to be contained in a single document"); *Eardman v. Bethlehem Steel Corp. Employee Welfare Benefit Plans*, 607 F. Supp. 196, 207 (W.D.N.Y. 1985) ("an employee benefit plan under ERISA can be comprised of more than one document"); *Myron v. Trust Co. Bank Long Term Disability Benefit Plan*, 522 F. Supp. 511, 519 (N.D. Ga. 1981) (finding "no authority that states that this written instrument [establishing an employee benefit plan, as referenced in 29 U.S.C. § 1102(a)(1)] must be one all-inclusive document"), *aff'd mem.*, 691 F.2d 510 (11th Cir. 1982), *cert. denied*, 462 U.S. 1119 (1983).

Because the Committee minutes were conclusive and binding under the terms of the Cluett Plan, the Second Circuit properly accorded them the status "plan documents" and held that no amendment was necessary for the Committee to adopt the PBGC-based floating rate. *See infra* Point VI.

C. The Second Circuit's Opinion Does Not Undermine The Distinction Between An Employer As Fiduciary And An Employer As Plan Amender

Petitioners' attempts to make the "distinction between discretionary management or administrative action and plan design or amendment" (Pet. 12) relevant to the present case are unavailing. While employers do not act as fiduciaries in amending their plans,[10] in this case, the change in the discount rate was not an amendment. To the extent that the Committee's decision was subject to ERISA's fiduciary duties, the Committee fulfilled those duties by acting on the considered advice of the plan actuary, R. App. 72a-73a, and Petitioners abandoned their claim for breach of fiduciary duty on appeal. P. App. 21a n.13. To the extent that the Committee's decision is viewed as a discretionary act of management, the alternative mechanism urged by Petitioners — amendment of the Cluett Plan by WestPoint's Board — would entail far greater management discretion, unconstrained by any requirement of a recommendation from the Cluett Plan's outside actuary.

V.

THERE IS NO CONFLICT AMONG THE CIRCUITS

Petitioners attempt to manufacture a conflict among the circuits where none exists.

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10. *See, e.g., Lockheed Corporation v. Spink*, 517 U.S. 882, 890-91 (1996); *Varity Corp. v. Howe*, 516 U.S. 489, 505 (1996).

A. The Second Circuit's Decision Does Not Conflict With *Dooley v. American Airlines, Inc.*

The Second Circuit *followed* the holding in *Dooley v. American Airlines, Inc.*, 797 F.2d 1447, 1451-52 (7th Cir. 1986), *cert. denied*, 479 U.S. 1032, 1087 (1987), that exercising or applying a provision of the plan does not equal an "amendment" to the plan under ERISA. P. App. 29a-30a. That holding does not give rise to a conflict; indeed, the Second Circuit cited four other federal decisions in accord. P. App. 30a.

Further, the Second Circuit's decision does not conflict with *Dooley*'s statement that American Airlines' plan was not in compliance with Revenue Ruling 79-90. The Cluett Plan is different because it expressly provided that "decisions and . . . records of the Committee shall be *conclusive and binding* upon the Company, Participants, and all other persons having any interest under the Plan." R. App. 65a-66a § 9.6. The Second Circuit properly held that this language gave duly-adopted minutes of the Committee the status of "plan documents" under ERISA. P. App. 31a.

The *Dooley* plan apparently contained no analogous clause, and the *Dooley* court *declined to rule* on the circumstances under which American Airlines' informal bulletins changing the discount rate could constitute plan documents. *Dooley*, 797 F.2d at 1451 n.6 ("The parties have briefed and argued whether the actuarial assumptions — contained, as they were, in bulletins which were physically distinct from the pension plan document — can be construed as part of the pension plan for purposes of ERISA. Because of our disposition of this case, we need not reach that question.").

B. The Second Circuit's Decision Does Not Conflict With *Frank v. Colt Industries, Inc.*

The other putative conflict raised by Petitioners should not even be addressed by this Court because it involves *Frank v. Colt Industries, Inc.*, 910 F.2d 90 (3d Cir. 1990), a case not cited in any of Petitioners' briefs in the Second Circuit, including their motion for reargument.

First, the Supreme Court's "normal practice . . . is to refrain from addressing issues not raised in the Court of Appeals." *Equal Employment Opportunity Commission v. Federal Labor Relations Authority*, 476 U.S. 19, 24 (1986) (writ of certiorari dismissed).[11] This case presents no ground for departing from that practice.

Second, the Second Circuit's opinion is fully consistent with *Frank*. In *Frank*, the Third Circuit held that, "[w]here an employer has created an integrated document" setting forth the terms of a benefit plan, "not every internal document containing a reference to management's interpretation of the plan should be regarded as a part of the plan itself." *Id.* at 98. As the Third Circuit's language suggests, *some* documents extrinsic to the written plan *may* form a part of the plan for ERISA purposes. The Court of Appeals below properly recognized that the Cluett Committee minutes constituted such a document, because the Cluett Plan referenced the Committee's documents and records and conferred upon them "*conclusive and binding*" status. P. App. 31a; R. App. 66a § 9.6. As is apparent from § 9.6's

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11. *Accord City of Springfield, Massachusetts v. Kibbe*, 480 U.S. 257, 259 (1987) (the Supreme Court "ordinarily will not decide questions not raised or litigated in the lower courts.") (writ of certiorari dismissed); *Rogers v. Lodge*, 458 U.S. 613, 628 n.10 (1982) (the Supreme Court refused to address "contention [that] was not properly raised in the Court of Appeals and was not addressed by that court.").

incorporation of extrinsic documents, the Cluett Plan was *not* an "integrated document" of the sort discussed in *Frank*. Indeed, the Cluett Plan contained no integration clause.

VI.

THE DECISION BELOW WAS CORRECT

A. The Committee Acted Under Its Express Authority To Change The Discount Rate

Petitioners have ignored the effect of § 9.6 of the Cluett Plan, which expressly conferred upon the Committee the power to adopt new actuarial assumptions. That section bears quoting in full:

> Authority and duties of the Committee:
>
> The Committee shall from time to t[i]me establish rules for the administration of the Plan and the transaction of its business. Except as herein otherwise expressly provided, the Committee shall have *the exclusive right* to interpret the Plan and *to decide any matters arising thereunder* in connection with the administration of the Plan. It shall endeavor to act by general rules so as not to discriminate in favor of any person. *Its decisions and the records of the Committee shall be conclusive and binding upon the Company, Participants, and all other persons having any interest under the Plan.*
>
> *The Committee shall adopt from time to time actuarial tables to be used as the basis for all actuarial calculations and shall determine from time to time the percentum rate or rates of interest to be used as the basis for calculations required in*

> *connection with the Plan*. As an aid to the Committee, the Actuary appointed by the Committee shall make annual actuarial valuations of the assets and liabilities of the Plan and shall certify to the Committee the tables and rate or rates of interest which he would recommend for use by the Committee. The Committee shall receive and review the periodic valuation of the Plan made by the Actuary.

R. App. 65a-66a § 9.6.

Similarly, § 1.3 of the Cluett Plan specifically provided for the actuarial factors to be set by the Committee:

> "Actuarial Equivalent" means an amount of equal value when computed on the basis of interest, mortality and other tables *as shall be adopted from time to time by the Committee on the advice of the Actuary*, the current factors being as specified below: . . . .

R. App. 65a § 1.3. Therefore, Section 1.3 of the Cluett Plan did not freeze the discount rate at 5%. Rather, it recited that 5% was among the Plan's "current" actuarial assumptions, and set forth a mechanism for the Committee to change those assumptions.

The Committee properly executed its powers under sections 1.3 and 9.6 when it changed the discount rate on February 16, 1989. The Committee received a written recommendation from the Actuary, implemented the Actuary's advice, and formally recorded its action in written minutes. R. App. 24a-25a, 72a-73a, 74a. Therefore, the discount rate was effectively changed and the PBGC-based rate was incorporated by reference into the EPI Amendment.

B. The Committee's Action Did Not Violate ERISA

The provisions of ERISA relied upon by Petitioners require that employee benefit plans: (i) be established and maintained pursuant to written instruments, 29 U.S.C. § 1102(a)(1); (ii) specify the basis on which payments are made to and from the plan, 29 U.S.C. § 1102(b)(4); and (iii) provide a procedure for amending the plan and identify the persons with authority to amend the plan, 29 U.S.C. § 1102(b)(3).

WestPoint did not violate any of those provisions: the Committee's February 16, 1989 action was taken pursuant to express provisions of the Cluett Plan, and was memorialized in the Committee's minutes. Under § 9.6 of the Cluett Plan, those minutes were a "conclusive and binding" plan document. *Accord Ravenscraft v. Hy-Vee Empl. Benefit Plan*, 85 F.3d 398, 401 (8th Cir. 1996) (plan's trust agreement conferred status of "Plan Document" on separate schedule of benefits); *see also Board of Trustees v. Weinstein*, 107 F.3d 139, 145-46 (2d Cir. 1997) (actuarial reports were not "instruments" under ERISA's the disclosure provision because they were not "governing documents" under which plan was established or operated). The adoption of the PBGC-based rate in a plan document or instrument rendered use of the Cluett Plan's written amendment procedure unnecessary.

CONCLUSION

For the reasons set forth above, the petition for writ of certiorari should be denied.

Respectfully submitted,

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November 6, 1998

APPENDIX

APPENDIX A — MEMORANDUM OPINION OF THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK DATED JANUARY 2, 1996

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

90 CIV. 3841 (SAS)
89 CIV. 2016 (SAS)

GORDON E. ALLEN, JOHN CURRIER, JAMES J. DUNNE, LEO FORNERO, GERARD P. MANDRY, NORMAN K. MATHESON, BRUCE E. MOORE, NICHOLAS PALLOTA and COCHRAN B. SUPPLEE,

Plaintiffs,

-against-

WESTPOINT-PEPPERELL, INC., D. MICHAEL ROARK, C. POWERS DORSETT and BARRY F. SHEA,

Defendants.

ROBERT D. KRUMME,

Plaintiff,

-against-

WESTPOINT-PEPPERELL, INC.,

Defendant.

MEMORANDUM OPINION

Appendix A

SHIRA A. SCHEINDLIN, U.S.D.J.:

This opinion addresses the question: when did a "Change in Control" of WestPoint-Pepperell, Inc. ("WestPoint") occur, as that term is used in a document known as the "EPI Amendment." A two day bench trial was held on this question. For the reasons set forth below, I conclude that a "Change in Control" occurred on April 5, 1989.[1]

A. Factual Background

In 1975, Cluett Peabody & Co. ("Cluett"), which was acquired by Defendant WestPoint in 1986, established an employee benefit program for its senior executives known as the Executive Permanent Insurance Program ("EPI Program"). This program consists of certain retirement and life and health insurance benefits, including a deferred compensation agreement which provides supplemental pension benefits. Plaintiffs are participants in the EPI program and are parties to a deferred compensation agreement under that program.

On July 29, 1987, the WestPoint Board of Directors approved various amendments to its employee benefit plans that accelerated the payment of benefits in the event a "Change in Control" of WestPoint occurred. On the next day, the Cluett Board of Directors, which was comprised of members of WestPoint's management, approved an EPI amendment with a

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1. Familiarity with the many prior opinions in this case is assumed. *See Allen v. WestPoint-Pepperell, Inc.*, 945 F.2d 40 (2d Cir. 1991); *Allen v. West Point-Pepperell, Inc.*, 1995 WL 649929 (S.D.N.Y. Nov. 2, 1995); *Allen v. WestPoint-Pepperell, Inc.*, 1991 WL 8505 (S.D.N.Y. Jan. 29, 1991), *rev'd*, 945 F.2d 40 (2d Cir. 1991).

Appendix A

"Change in Control" definition identical to the WestPoint amendments.[2]

As approved in 1987, the "Change in Control" provisions provided that a "Change in Control" would occur if a person or group of persons became the "Beneficial Owner" of 30% of WestPoint's stock, "unless a majority of the continuing Directors of the Board determines in their sole discretion that, for purposes of the Plan, a Change in Control has not occurred." Thus, under this language, the Board retained discretion to declare that a "Change in Control" did not occur.

Although the "Change in Control" amendment to the EPI plan was approved in July 1987, it was not implemented until November 1988. By that time, pursuant to the advice of outside counsel, the provision had been changed in two respects. First, the percentage of stock that was needed to trigger a "Change in Control" was reduced from 30% to 20%. Second, the Board's discretion to declare that a "Change in Control" had not occurred was eliminated. This last change was apparently made because of concerns that a third party might condition a tender offer on the Board finding no "Change in Control," thereby forcing the Board to choose between money for its shareholders and the protection of its employees. *See* Def. Trial Ex. U.

As noted, under the EPI Amendment implemented on November 11, 1988, a "Change in Control" occurs if a person or group of persons becomes the "Beneficial Owner" of 20% or more of WestPoint's stock. Subsection (f) of Section 4A(1) of the Amendment defines the term "Beneficial Owner":

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2. This acceleration would result in the payment of a single lump sum benefits rather than future monthly payments.

> by reference to Rule 13d-3 under the Act as such Rule is in effect on June 24, 1987, provided, however, that any individual, corporation, partnership, group, association, or other person or entity which has the right to acquire any of WestPoint's outstanding securities entitled to vote generally in the election of directors at any time in the future, *whether such right is contingent or absolute*, pursuant to any agreement, arrangement, or understanding or upon exercise of conversion rights, warrants or options, or otherwise, shall be deemed the Beneficial Owner of such securities.

Joint Exhibit 18 ¶ 4A(l)(f) (emphasis added).

On October 24, 1988, Farley, Inc. and its subsidiaries ("Farley") initiated a hostile tender offer for all of the shares of WestPoint. For several months, WestPoint vigorously contested Farley's takeover attempt, and, in early February 1989, decided to "auction" the company to the highest bidder. On February 23, 1989, after Farley submitted the highest bid, WestPoint entered into a merger agreement with Farley. On April 5, 1989, Farley purchased approximately 95% of WestPoint's stock pursuant to its tender offer. On that same day, pursuant to the EPI Amendment, WestPoint sent each of the *Allen* plaintiffs a lump sum payment.

At trial, Plaintiffs argued that a "Change in Control" occurred under the EPI Amendment long before April 5, 1989, the date on which Farley actually purchased the bulk of WestPoint's stock. Plaintiffs note that, under the EPI Amendment, one is considered the "Beneficial Owner" of any stock one has the "right to acquire," even where this right is

"contingent." Plaintiffs argue that, prior to April 5, Farley had a contingent right to acquire any stock that had been tendered to it. Accordingly, Plaintiffs contend that a "Change in Control" occurred under the EPI Amendment by November 21, 1988, when the stock Farley owned, combined with the shares that had been tendered to it, exceeded 20%.[3]

Defendants argue that Plaintiffs' interpretation of the "Change in Control" provision is contrary both to the language of the Amendment and to the intent of the Board in creating this provision. Moreover, they assert that Plaintiffs' interpretation should be avoided because it would create the absurd result of a "Change in Control" clause which does not fulfill any of the functions associated with such provisions.

B. The Plain Language

In interpreting a contract, the Court strives to effectuate the intent of the contracting parties "as revealed by the language they chose to use." *Seiden Assocs. v. ANC Holdings, Inc.*, 959 F.2d 425, 428 (2d Cir. 1992). Where the contract's language is unambiguous, " 'its meaning must be determined from the four corners of the instrument without resort to extrinsic evidence of any nature.' " *Goodheart Clothing Co. v. Laura Goodman Enterprises, Inc.*, 962 F.2d 268, 272 (2d Cir. 1992) (quoting John D. Calamari & Joseph M. Perillo, *Contracts* 166-67 (3d ed. 1987)).

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3. Alternatively, Plaintiffs contend that the execution of a Merger Agreement, which Farley and WestPoint entered into on February 23, 1989, triggered the "Change in Control" provision. Plaintiffs note that the Agreement gave Farley the right to acquire all remaining shares of the company once a majority of the shares were tendered to him. Thus, they argue that the Agreement gave Farley the "contingent" right to acquire up to 49% of WestPoint's shares.

In the case at hand, each party has offered an initially plausible interpretation of the EPI Amendment's text. As noted, Plaintiffs contend that, under the Amendment's language, Farley became a "beneficial owner" of more than 20% of WestPoint's stock because it had a "contingent" right to purchase stock that was tendered to it in November. Under Plaintiffs' theory, Farley's right was "contingent" on the shareholders not withdrawing the stock they had tendered, which they had the right to do until April 5, 1989. Trial Transcript ("Tr.") at 379-80.[4]

Defendants argue that Plaintiffs' interpretation of the word "contingent" is too expansive, and eviscerates the significance of the phrase "right to acquire." Defendants note that the word "right" "connotes an ascertainable and legally enforceable power." *United States v. Byrum*, 408 U.S. 125, 136, 92 S. Ct. 2382, 2390 (1970). They contend that, because the shareholders had the power to withdraw their tendered shares at all times, Farley never had any legally enforceable right to purchase them.[5]

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4. Plaintiffs note that Farley's October, 1988 Letter of Transmittal to WestPoint's shareholders provides that tender of the shares will constitute a "binding agreement." *See* Plaintiffs' Trial Ex. 83. This language had no affect, however, on the tendering shareholders' absolute right to withdraw the tender of their stock at any time prior to the expiration of the offer. Indeed, earlier in the sentence quoted by plaintiffs, the letter states that the tender is "subject to the conditions of the Offer. . . .

5. Plaintiffs respond by citing a number of cases that stand for the proposition that one party's "restricted option to terminate" an agreement does not destroy the validity of the agreement. *See, e.g., Dorman v. Cohen*, 413 N.Y.S.2d. 377, 382 (1st Dep't 1979); *Satenstein v. Satenstein*, 248 N.Y.S.2d. 281 (Sup. Ct. N.Y. Co. 1963), *aff'd*, 247 N.Y.S.2d 380

(Cont'd)

Defendants also emphasize that the first part of the definition of "Beneficial Owner" refers to SEC Rule 13d-3. They argue that the term "right to acquire," as used in that Rule, refers to contractual, or legally enforceable, rights. *See* Testimony of Defendants' Expert Witness, Professor Bernard Black, Tr. at 329. They note that under Rule 13d-3 there are situations in which one may be the "Beneficial Owner" of stock one has a contingent contractual right to purchase. *See, e.g., Newmark v. RKO General*, 425 F.2d 348, 356 (2d Cir.), *cert. denied*, 400 U.S. 854, 91 S. Ct. 64 (1970) (finding defendant to be beneficial owner where it contracted to purchase stock contingent on regulatory board's approval).[6] Defendants

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(Cont'd)
(1st Dep't 1964). In the instant action, however, the shareholders' right to withdraw their shares was absolute. As long as they acted before the expiration of their withdrawal rights, the shareholders were free to withdraw at will. They did not have to give *prior* notice to Farley, but merely had to fill out a simple form, and deliver it to a location specified in the tender offer documents. Tr. at 380. Accordingly, they had no legally enforceable obligation. *See Dorman*, 413 N.Y.S.2d at 382-83. Because the shareholders option to withdraw went "so far as to render illusory the promise of the party having the option, there is indeed no consideration, and therefore no contract." 3 Williston § 7:14 (4th ed. 1992).

There is another reason the cases cited by Plaintiffs are distinguishable. Those cases involve a party's right to terminate an existing and ongoing contract, to halt performance that has already been partially completed. Here, the shareholders were empowered to withdraw their shares before either party had initiated performance. Moreover, because there was a possibility that the tender offer would fail, it was feasible that, even absent withdrawal, neither party would ever be required to perform.

6. Although *Newmark* involved Section 16(b) of the Securities Exchange Act, because the definition of "Beneficial Owner" is even broader under Rule 13d-3, the case has precedential value in interpreting that Rule.

acknowledge that the addition of the word "contingent" in the EPI Amendment must encompass something broader than provided for in the Rule. Tr. at 372-73. However, they contend that it cannot be read to embrace the mere tendering of shares by persons retaining the power of withdrawal, which creates no contractual rights.

The Court finds that each party has offered a textually plausible interpretation, and that the EPI Amendment's language is ambiguous. Ambiguity exists where a contract's language is:

> capable of more than one meaning when viewed objectively by a reasonably intelligent person who has examined the context of the entire integrated agreement and who is cognizant of the customs, practices, usages and terminology as generally understood in the particular trade or business.

Walk-In Medical Centers, Inc. v. Breur Capital Corp., 818 F.2d 260, 263 (2d Cir. 1987) (quotation omitted). Here, each party's interpretation finds some support in the text, and is buttressed by credible expert testimony. Moreover, the Second Circuit has previously expressed its view that this language is ambiguous. *See Allen v. WestPoint-Pepperell, Inc.*, 945 F.2d 40, 46 (2d Cir. 1991) (noting that determining the "Change in Control" date in this case presents a question of fact).

C. Intent

Where a contract's language is ambiguous, a court may look to extrinsic evidence of the parties' intent to construe its meaning. *See Hudson-Port Ewen Assocs. v. Chien Kuo*, 78

N.Y.2d 944, 945, 573 N.Y.S.2d 637 (1991). At trial, Defendants offered evidence aimed at demonstrating that WestPoint did not intend to create a "Change in Control" provision that could be triggered by the mere tendering of shares. Although the Court finds that this evidence was not dispositive, it did tend to support the Defendants' position.

For example, Defendants produced a letter dated June 19, 1987 from C. Powers Dorsett, WestPoint's Secretary and General Counsel, to the members of the Compensation Committee of WestPoint's Board. In the letter, Mr. Dorsett, who reviewed the existing employee benefit plans at the Board's behest, recommends some changes. *See* Def. Trial Ex. JJ. Addressing the concept of a "Change in Control," Mr. Dorsett wrote that it could be defined as "the *acquisition* by someone of a stated percentage of the Company's stock." *Id.* (emphasis added). Nowhere in this letter, which is dated a month prior to the Board's approval of the "Change in Control" language, did Mr. Dorsett mention anything approximating the definition of "Change in Control" advocated by the Plaintiffs here.

Indeed, after years of discovery, the Plaintiffs were not able to produce any evidence that anyone associated with, or consulted by, WestPoint believed that the "Change in Control" provision they were adopting could be triggered by the tendering of shares. Ordinarily, the Court would accord little significance to this absence of any evidence of intent. However, the evidence at trial revealed that nobody involved in this case, not even Plaintiffs' own expert, had ever previously seen a "Change in Control" provision that could be triggered by the tendering of shares. Tr. at 423. If WestPoint intended to adopt such an unprecedented provision, it is likely that some documentary or testimonial evidence would exist to this effect.

In addition, WestPoint's conduct after the adoption of the "Change in Control" language is at odds with Plaintiffs' interpretation. Conduct subsequent to the date of the contract is relevant in discerning WestPoint's intent. *See Granite Computer Leasing Corp. v. Travellers Indemnity Co.*, 1987 WL 8647, *3 (S.D.N.Y. Apr. 1, 1987) (relevant extrinsic evidence includes "the parties' own practical interpretation of the contract, manifested by their conduct subsequent to the contract's formation . . . before it became the subject of litigation"). WestPoint waited until April 5, 1989, the date Farley actually acquired more than 20% of its stock, to make any payouts. As Professor Black, Defendants' expert noted, there is no evidence that any members of the Board concluded in November: "the change of control provisions have been triggered, let's write large checks to ourselves." Tr. at 346. In fact, the transmittal letter the company sent to EPI Plan participants in November 1988, alerting them to the adoption of the EPI Amendment, does not mention Farley's existing tender offer, much less the possibility that the tender offer may have already caused the "Change in Control" provision to be triggered.

D. Context and Purpose

Although the evidence of intent weighs in favor of Defendants' interpretation, this limited evidence does not dispose of the issue before the Court. It is therefore necessary to examine the context of the formation of the contract, and the purpose it was intended to serve. *See Genet v. Delaware & Hudson Canal Co.*, 163 N.Y. 173, 179 (1900). Such an examination reveals that Defendants' interpretation is preferable to that offered by Plaintiffs.

Appendix A

The testimony at trial revealed that there are two principal purposes (other than deterring potential raiders) for putting a "Change in Control" provision in an employee benefit plan. The first is to assure employees that they will be paid in the event of a takeover by depriving a raider of the power to prevent payment. Tr. at 416, 426. The second is to insure that key employees will be able to focus on their jobs during the hectic period associated with a potential takeover, rather than having to worry about how they will pay their bills if they lose their jobs. Tr. at 416.

Plaintiffs' interpretation makes little sense in light of these purposes. Arguably, the first purpose is served by either interpretation of the clause. However, it makes much more sense to pay large sums to employees after control has actually changed, rather than before, when the takeover plan may still fail.[7] Paying out large sums during a takeover battle could drain a company of cash during a time when money is particularly tight. Indeed, Defendants' expert testified that such an early payout could violate the Board's fiduciary duty to act in the best interests of the shareholders. Tr. at 359.[8] Moreover, the

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7. Obviously, tender offers are not always successful. In such instances, it would make little sense for a company to have prematurely made lump sum payouts to its employees. Indeed, one purpose of deferred compensation is to delay payment to employees until they have retired, when they will presumably be in a lower tax bracket. In the context of a failed tender offer, premature payouts would unnecessarily defeat this purpose.

8. One of the benefit plans protected employees from dismissal for two years after a "Change in Control" occurred. An early payout would be particularly senseless under this plan. Such a payout would prematurely trigger this provision, and provide a smaller window of protection once a tender offeror assumed actual control. Tr. at 430-32.

second purpose would be completely thwarted by giving effect to Plaintiffs' interpretation. By paying out lump sums to its executives while a takeover battle is still being waged, a company would encourage its key employees to retire at the time they are most needed.

Additionally, because the Amendment provided that WestPoint had to make payments upon a "Change in Control," it was vital that WestPoint be able to discern when such a change occurred. Yet, under the interpretation urged by Plaintiffs, there is no reason WestPoint would know exactly when enough shares had been tendered to Farley to trigger the "Change in Control." The securities laws only require a tender offeror to disclose how many shares have been tendered to it on the date the shareholders' right to withdraw expires. They do not require such disclosure on a day to day basis. Tr. at 343. Hence, under Plaintiffs' interpretation, WestPoint could not have known precisely when it was obligated to make payouts to its employees.

There are other reasons Plaintiffs' interpretation does not make sense when viewed with regard to the overall context and purpose behind the "Change in Control" provision. The "Change in Control" provision was only one of WestPoint's anti-takeover devices. The company had also adopted a "poison pill" provision, which used standard language drafted by lawyers at Wachtell, Lipton, Rosen & Katz. This provision explicitly stated that it could not be triggered by the mere tendering of shares to a tender offeror. As Defendants' expert, Professor Black, pointed out, one would expect these anti-takeover devices to work together, rather than to be triggered at completely different times. Tr. at 358.

Plaintiffs' interpretation would give the term "Beneficial Owner" a meaning at odds with common sense, and with the purpose and context behind the "Change in Control" provision. Linguistically, it seems odd to say that Farley was the "Beneficial Owner" of shares in which he had no economic interest, shares that could be withdrawn by their actual owners any time before April 5, 1989. Because such an awkward interpretation also conflicts with the purpose behind a "Change in Control" provision, it should be avoided. Given this context, it makes no sense to say that Farley had a "contingent" right to purchase the stock which it had been tendered.

Certainly, the word "contingent" in the EPI Amendment must have some significance. However, it cannot be read to embrace the possibility of tendering shareholders withdrawing their stock before it could be purchased. Such a putative "contingency" is different in kind from the contingencies recognized under Rule 13d-3, and incompatible with the notion of a "right to acquire." The contingencies embraced by Rule 13d-3 involve occurrences beyond either party's complete control, in situations in which there is a legally enforceable contract between the parties. *See Newmark*, 425 F.2d at 356 (right to acquire stock contingent on regulatory approval); *In re Coca Cola Bottling Company*, Exchange Act Release No. 13655, 12 SEC Docket 927, 1977 SEC LEXIS 1469 (June 21, 1977) (Coca Cola's right to purchase shares contingent on its not reaching merger agreement with third party). Here, the shareholders had complete control over the alleged "contingency," and Farley never had any legal right to their tendered stock.

A contract should be construed in light of its objective, and should not be read in a fashion that defeats its purpose. *See*

Appendix A

Cromwell Towers Redev. Co. v. City of Yonkers, 41 N.Y.2d 1, 6 (1976). Defendants' interpretation, that a "Change in Control" occurred on April 5, 1989, when Farley had actual control of over 20% of WestPoint's stock, adheres to this purpose. Plaintiffs' view is rejected as it conflicts with the purpose of a "Change in Control" provision and would bring about an absurd result.[9] *See Westbury Post Ave. Assoc. v. Great Atlantic & Pacific Tea Company, Inc.*, 361 N.Y.S.2d 377 (1st Dep't 1974). The Court therefore holds that a "Change in Control," as used in the EPI Amendment, occurred on April 5, 1989.

SO ORDERED:

Shira A. Scheindlin
U.S.D.J.

Dated: New York, New York
January 2, 1996

9. The Court also rejects Plaintiffs' alternative argument that the Merger Agreement triggered a "Change in Control" on February 23, 1989. The execution of the Agreement certainly increased the likelihood that Farley would acquire 20% of WestPoint's shares. However, it did not in any way diminish the shareholders' right to withdraw the shares they had tendered. Tr. at 367. Accordingly, the Merger Agreement did not trigger a "Change in Control."

APPENDIX B — OPINION AND ORDER OF THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK DATED MAY 13, 1996

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

90 Civ. 3841 (SAS)
89 Civ. 2016 (SAS)

GORDON E. ALLEN, JOHN CURRIER, JAMES J. DUNNE, LEO FORNERO, GERARD P. MANDRY, NORMAN K. MATHESON, BRUCE E. MOORE, NICHOLAS PALLOTA and COCHRAN B. SUPPLEE,

Plaintiffs,

-against-

WESTPOINT-PEPPERELL, INC., D. MICHAEL ROARK, C. POWERS DORSETT and BARRY F. SHEA,

Defendants.

ROBERT D. KRUMME,

Plaintiff,

-against-

WESTPOINT-PEPPERELL, INC.,

Defendant.

OPINION AND ORDER

Appendix B

SHIRA A. SCHEINDLIN, U.S.D.J.:

This opinion addresses two issues vital to the resolution of these actions: (1) whether the releases executed in connection with the *Allen* Plaintiffs' lump sum payouts under the EPI Amendment should be rescinded, and (2) whether Plaintiffs are entitled to have their attorneys' fees paid by Defendant West Point-Pepperell, Inc. The Court held a bench trial from January 3 to January 9, 1996 on these issues. The Findings of Fact and Conclusions of Law set forth below are based on this trial and a two day bench trial held December 27-28, 1995 on related issues.

I. *Background*

A. *Parties*

The Plaintiffs in this action are former executives of Cluett Peabody & Co. ("Cluett"), an apparel manufacturer which was acquired by Defendant WestPoint-Pepperell, Inc. ("WestPoint") in 1986. WestPoint is a Georgia corporation conducting business in textile, apparel and bed products. Cluett was merged into WestPoint in January 1989 and operated as a division of WestPoint until March 1990, when Cluett was sold to Bidermann Industries, Inc.

Defendant D. Michael Roark ("Roark") was Vice President of Human Resources for Cluett at all relevant times until 1986, and then Vice President of Human Resources for WestPoint until May 1989. Defendant C. Powers Dorsett ("Dorsett") was, at all relevant times, WestPoint's General Counsel. Defendant Barry F. Shea was Assistant Treasurer and then Treasurer of WestPoint, and a member of the Cluett Retirement Plan

Committee. Patrick Walsh ("Walsh"), not a party to this action, was, at all relevant times, Assistant Treasurer of Cluett, and the day-to-day administrator of the Executive Permanent Insurance Program ("EPI Program").

B. *Factual Background*

In 1975, Cluett established for its senior executives an employee benefit program known as the EPI Program. This program consists of retirement and life and health insurance benefits, including a deferred compensation agreement which provides supplemental pension benefits. Plaintiffs are participants in the EPI program and are parties to a deferred compensation agreement under that program.

On July 29, 1987, WestPoint's Compensation Committee recommended that Cluett's Board adopt a "Change in Control" amendment to the EPI Plan (the "EPI Amendment"), which would provide EPI participants with a lump sum payment upon a "Change in Control" of WestPoint. Cluett's Board approved the EPI Amendment on July 30, 1987, although it was not finalized until November 1988. On November 11, 1988, the EPI Amendment was circulated to the EPI participants; within a few weeks, Plaintiffs all returned executed copies of this Amendment.

In late 1988 and early 1989, WestPoint took steps to change the discount rate used to calculate the lump sums that EPI participants would receive if a "Change in Control" occurred. The EPI Amendment referred to the actuarial assumptions contained in the Cluett Employee Retirement Plan ("Cluett Pension Plan"), which provided for a 5% discount rate. WestPoint sought to make this rate conform to that used in the

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WestPoint Employee Retirement Plan ("WestPoint Pension Plan"), which provided for a discount rate based on rates published by the Pension Benefit Guaranty Corporation ("PBGC"). Accordingly, the Cluett Pension Plan Committee ("Cluett Committee") met on February 16, 1989 and purported to adopt a PBGC-based rate for the Cluett Pension Plan.[1]

The following week, Roark sent each EPI participant a letter, dated February 22, 1989, advising that lump sum payments would be calculated using a PBGC-based rate of 9.3%. Accompanying this letter was an election form which gave the participants two choices: (1) they could receive the lump sum payment based on the PBGC-based rate and release WestPoint from any further obligation; or (2) they could revoke the November 11, 1988 EPI Amendment and forfeit the right to receive a lump sum payment. Each of the *Allen* Plaintiffs checked a box indicating that he was selecting the first option, and returned the form to Roark.[2] On or about April 5, 1989, the *Allen* Plaintiffs each received a lump sum payment calculated using a 9.3% discount rate.

In an Opinion and Order dated November 2, 1995, I held that the Cluett Committee had no authority under ERISA to change the discount rate contained in the Cluett Pension Plan. *See Allen v. West Point-Pepperell, Inc.*, 908 F. Supp. 1209,

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1. The group that met on February 16, 1989 consisted of the members of the WestPoint Management Pension Committee. In 1988, the WestPoint Management Pension Committee was appointed by the Cluett Board of Directors to act as the Cluett Committee. *See Allen v. West Point-Pepperell, Inc.*, 908 F. Supp. 1209, 1214 (S.D.N.Y. 1995). Thus, this group acted as the Cluett Committee at its February 16 meeting.

2. Plaintiff Robert Krumme refused to sign the release.

1222 (S.D.N.Y. 1995). "Accordingly, the 5% discount rate printed in the Cluett Pension Plan was never validly changed and was at all relevant times one of the actuarial assumptions 'contained in' the Cluett Pension Plan for purposes of the EPI Amendment." *Id.* at 1222-23.

The *Allen* Plaintiffs now seek rescission of the releases they executed in early 1989. They contend that rescission is appropriate because the releases were the product of a "mutual mistake" on the part of WestPoint and themselves concerning the discount rate contained in the Cluett Pension Plan. In addition, both the *Allen* Plaintiffs and Robert Krumme seek attorneys' fees pursuant to a provision contained in the EPI Amendment which provides that an executive will be paid or reimbursed for fees "[i]f at any time upon or after a change in control there should arise any dispute" concerning an interpretation of the EPI Amendment.

I. *Findings of Facts*

On January 27, 1987, the WestPoint Board of Directors discussed the possibility of amending its employee benefit plans to protect participants in the event the company experienced a change in control. The Board instructed management to review all employee benefit plans and to report back to the Board with its recommendations. *See* Minutes of January 27, 1987 Board meeting, Def. Ex. A. After management conducted such a review, Dorsett, WestPoint's General Counsel, presented his report and recommendations to the WestPoint Board's Compensation Committee on June 23, 1987. *See* Minutes of June 23, 1987 Compensation Committee Meeting, Def. Ex. KK. The Compensation Committee approved management's recommendations and resolved to present them to the full Board. *See id.*

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The Compensation Committee reported management's recommendations to the Board on June 24, 1987. With respect to the EPI Program, management recommended that "the present value of the benefit be paid by way of lump sum upon a change in control." Compensation Committee Report, Def. Ex. B. No specific method of determining present value was mentioned in management's recommendations; the intent was simply to provide "the fair present value that would be properly calculated with a realistic interest rate." Testimony of C. Powers Dorsett, General Counsel of WestPoint, Trial Transcript ("Tr.") 913.

In the month following the June 24, 1987 Board meeting, draft amendments to several of WestPoint's benefit plans (including the EPI Program) were prepared. These amendments were presented to, and approved by, the WestPoint Compensation Committee at a meeting on July 29, 1987. *See* Minutes of July 29, 1987 Compensation Committee Meeting, Def. Ex. C. At this time Cluett, although owned and controlled by WestPoint, still had its own Board of Directors. The Compensation Committee thus recommended to the Cluett Board that it adopt the proposed amendment to the EPI Program permitting lump sum payments in the event of a change of control. Tr. 916. On July 30, 1987, the Cluett Board authorized management to enact such an amendment. *See* Action of Cluett Board, Pl. Ex. 119.

A. *Drafting of the EPI Amendment*

Ronald Heller, then General Counsel of Cluett, prepared the initial draft of the EPI Amendment. Tr. 916. The draft provided for participants to receive, upon a change in control, the present value of their accrued EPI benefit, defined as the

"actuarial equivalent" of that benefit. Section 4A(l)(c) of the draft EPI Amendment defined "actuarial equivalent" as follows:

> The term "Actuarial Equivalent" means, with respect to an Accrued Benefit, any Deferred Compensation (or contingent Deferred Compensation, as the case may be) benefit provided under the terms of this Agreement which has the same present value as the Accrued Benefit. For the purpose of establishing whether a benefit is the Actuarial Equivalent of another benefit the actuarial assumptions contained in Cluett's Employee Retirement Plan shall be employed for so long as that Plan remains in existence and if such Plan is no longer in existence, the actuarial assumptions last used by such Plan shall be used.

This language was based on a change in control amendment to the WestPoint Supplemental Executive Retirement Plan (the "SERP Amendment"), which Heller used as a model in drafting the EPI Amendment. Tr. 918-19. Indeed, the definition of "actuarial equivalent" in the two amendments is identical except in one respect: where the SERP Amendment refers to the actuarial assumptions contained in WestPoint's Pension Plan, Heller referenced the assumptions contained in the Cluett Pension Plan. *Id.*

The actuarial assumptions in the Cluett Pension Plan had not been changed for many years and were outdated. The Plan provided for a discount rate of 5%, which was well below the market rate. When TPF&C, an actuarial services firm, became the Plan Actuary for the Cluett Pension Plan in 1986, it notified WestPoint of this problem and recommended that the PBGC

based rates used in the WestPoint Pension Plan be adopted for the Cluett Pension Plan. However, under the Cluett Pension Plan, lump sums were only payable in *de minimis* amounts;[3] accordingly, substantial sums were not at stake and WestPoint declined to assign a high priority to changing the actuarial assumptions. *See* Deposition of Steven A. Harrold, Vice President of TPF&C, dated July 27, 1989, at 100-01, 105-06, 107; Deposition of Steven A. Harrold, dated December 6, 1994, at 57-58, 113-16.

B. *Finalizing the EPI Amendment*

Although the change in control amendments to WestPoint's other benefit plans were implemented in 1987, this was not the case with the EPI Amendment. While working on the Amendment, Heller discovered that — under certain circumstances — it could result in payments duplicative of benefits provided under the EPI Program's life insurance policy. Without a ready solution to this problem, the WestPoint legal staff temporarily shelved the EPI Amendment. Tr. 921-22.

On October 24, 1988, Farley Inc. launched a takeover bid for WestPoint. Complaint ¶ 19. As a result of this action, WestPoint conducted a review of its unfunded employee benefit plans. During that review, management discovered that the EPI Amendment had never been finalized. Tr. 924. Dorsett then instructed Clay Humphries, a WestPoint attorney, to take the steps necessary to get the Amendment finalized. *Id.* Dorsett told Humphries to draft the EPI Amendment in a manner

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3. The discount rate in the Cluett Pension Plan was used only for calculating lump sums under $3,500. *See* Deposition of Steven A. Harrold, TPF&C Actuary, dated July 27, 1989, 101-02.

consistent with WestPoint's other change in control amendments. Tr. 1040.

Humphries obtained a copy of the Heller draft and hurriedly began finalizing it. Because he was completely unfamiliar with the EPI plan, Humphries was reluctant to make any substantive changes. Tr. 1013. Additionally, he did not know that the actuarial assumptions contained in the Cluett Pension Plan differed from those contained in the WestPoint Pension Plan; thus, although he had been instructed to make the EPI plan consistent with WestPoint's other plans, he left intact the Amendment's reference to the actuarial assumptions contained in the Cluett Pension Plan. Tr. 1017, 1019.[4]

After amending the Heller draft, Humphries sent a copy of it to Walsh to get his comments. On November 10, 1988, Walsh wrote to Humphries suggesting that the definition of "Actuarial Equivalent" in Section 4A(1)(c) of the draft Amendment be revised to specify that an interest rate of 5% would be used to calculate the present value of future EPI benefits. *See* Undated Draft Amendment, Joint Ex. 6; Walsh Memo, dated November 10, 1988, Joint Ex. 15. Humphries rejected Walsh's suggestion that the discount rate be spelled out because he wanted all change in control amendments to be consistent. He sent Walsh a handwritten note that stated:

> I think we need to adopt the amendment as it is drafted if at all possible, for the sake of uniformity.

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4. It is unclear whether Humphries even noticed that the Heller draft referred to the Cluett Pension Plan's actuarial assumptions. In any event, he testified that "it wouldn't have jumped out at me, because as far as I was concerned [the Cluett and WestPoint Pension Plans] used the same rates." Tr. 1019.

> We have several plans with these amendments and I would like for them to all read alike.

Joint Ex. 15.

When Humphries rejected Walsh's suggested revision, he still did not realize that the actuarial assumptions contained in the Cluett Pension Plan differed from those in the WestPoint Pension Plan. Tr. 1017. He thought he remembered being told by an actuary that the plans all used the same actuarial assumptions. Tr. 1018-19. Moreover, because Humphries had no familiarity with the concept of discount rates, the 5% rate in Walsh's suggested revision did not attract his attention. Tr. 1017. At trial, Humphries expressed regret for his oversight: "I have spent many sleepless nights concerned that I was the one most able to catch this mistake and didn't do it, and all this would have been for naught." *Id.*

On November 11, 1988, the EPI Amendment was circulated to the EPI participants under a cover letter. Consistent with the Board's intent, the cover letter stated that the EPI Amendment would provide for payment "of the present value of the benefits called for under the (Deferred Compensation] Agreement." *See* Letter from Patrick Walsh to EPI Participants, Joint Ex. 19. Each of the Plaintiffs returned an executed copy of the EPI Amendment to Walsh within a few weeks of receiving it.

C. *WestPoint Discovers the Error*

In early February 1989, Roark learned from Walsh that a 5% discount rate would be used to calculate lump sums under the EPI Amendment. Tr. 1065. The news came as a shock to Roark and was of great concern to him. He was troubled because

the Chairman of the Board had instructed management to make the methodology used under the various amendments consistent, and Roark had assured members of the board that this would be done. Tr. 1065-66, 1111. Additionally, Roark believed that a 5% discount rate was "totally inappropriate" given the high interest rates that prevailed at the time. Tr. 1070-71. Indeed, in February 1989, even the interest rate on a 30-year Treasury Bill — a very conservative investment — exceeded 9%. *See* Federal Reserve Statistical Release, Def. Ex. I.

Roark notified WestPoint management that the discount rate referenced in the EPI Amendment was different from that referenced in WestPoint's other plans. After reviewing pertinent sections of the Cluett Pension Plan, WestPoint management determined that the discount rate could be changed by the Cluett Committee (then consisting of members of the WestPoint Management Pension Committee) on the advice of the Plan Actuary. Management believed that if the Plan Actuary agreed that the actuarial assumptions contained in the Cluett Pension Plan were outdated and unfair, the Cluett Committee could adopt new assumptions consistent with those in WestPoint's other plans.

TPF&C, the Plan Actuary, was asked its advice in this regard. On February 16, 1989, TPF&C recommended that new actuarial assumptions be adopted, and that the new assumptions be identical to those in the WestPoint Pension Plan. *See* Letter from Steven A. Harrold, dated February 16, 1989, Def. Ex. H(1). That same day, the Cluett Committee met and, pursuant to the Cluett Pension Plan, purported to adopt the actuarial assumptions recommended by TPF&C. *See* Minutes of February 16, 1989 Pension Committee Meeting, Def. Ex. H(2).

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Walsh had informed a number of EPI participants that any lump sum payments they received would be calculated using a 5% discount rate. Tr. 1069. WestPoint's management was concerned that some of those participants might have executed the EPI Amendment with that advice in mind. Tr. 1070. Accordingly, WestPoint decided to inform all EPI participants of the discount rate that would be used in calculating lump sum payments, and to give participants an opportunity to rescind the EPI Amendment if they did not desire a payout calculated with the new rate. Tr. 1069.

On February 22, 1989, Roark wrote to the EPI participants notifying them of the 9.3% rate and affording them the opportunity to rescind their November 11, 1989 EPI Amendments. Roark's letter expressly referred to the fact that some EPI participants "have told us they were led to believe that a 5% discount rate would be used to determine lump sum values." Letter from Roark to EPI Participants, dated February 22, 1989, Joint Ex. 22. Roark's letter appended an election form which required each participant to either (1) execute a release of WestPoint in order to be eligible for a lump sum payment or (2) rescind the EPI Amendment. The release contained the following language:

> I understand that the lump sum payment of the actuarial equivalent of my deferred compensation benefit will be in full satisfaction of all obligations of West Point-Pepperell, Inc., as successor to Cluett, Peabody & Co., Inc., under the terms of my Deferred Compensation Agreement, and that in accepting a lump sum payment I shall thereby release West Point-Pepperell, Inc., its directors, officers,

employees, and agents, and its successors and assigns, from all obligations under the Agreement.

Joint Ex. 22. Each of the *Allen* Plaintiffs executed the release.

The *Allen* Plaintiffs understood that the document they were signing released WestPoint from any further obligation to them. Tr. 545, 595, 630, 661, 734, 856, 868. They signed the release under the belief that 9.3% was the discount rate referenced in the EPI Amendment. Tr. 518-19, 566, 568-9, 613, 648, 719, 844, 862.[5]

On April 5, 1989, as a result of Farley's tender offer, a change in control of WestPoint took place and the *Allen* Plaintiffs were sent lump sum payments calculated using the 9.3% rate. When they received the lump sums, the *Allen* Plaintiffs did not feel they had any dispute with WestPoint; they believed they had been paid the full amount owed to them. Tr. 520-21, 570, 614, 648, 721, 647, 864, 880.

D. *Krumme*

Unlike the *Allen* Plaintiffs, Robert Krumme refused to sign the release sent on February 22, 1989. In fact, having heard rumors about the purported change in the discount rate, Krumme wrote a letter of protest to Dorsett one day before the release was sent out. In his letter, Krumme stated, *inter alia*, that he believed the proper discount rate was 5%. *See* Letter from Robert Krumme, dated February 21, 1989, Pl. Ex. 71. On March 1, 1989, Krumme sent a letter to Roark reiterating his view

5. Only Plaintiff James J. Dunne doubted whether 9.3% was the appropriate rate when he signed the release. *See* Telephonic Deposition of James J. Dunne, dated December 14, 1994, at 82.

that he was entitled to be paid at a 5% discount rate. *See* Letter from Robert Krumme, dated March 1, 1989, Pl. Ex. 73.

On March 8, 1989, Krumme wrote a third letter of protest. In this letter, which was addressed to Dorsett, Krumme threatened to take legal action against WestPoint. *See* Letter from Robert Krumme, dated March 8, 1989, Joint Ex. 23. On March 24, 1989, before the change in control payments were made, Krumme sued WestPoint. *See* Complaint in Krumme Action, Def. Ex. CC. Krumme's complaint alleged, *inter alia*, that the change in the discount rate was ineffective and that, if the Cluett Pension Plan had been amended, the amendment had been accomplished without proper authorization and implementation. *See id.* ¶¶28-33.

During the summer and fall of 1989, Krumme contacted several of the *Allen* Plaintiffs to encourage them to bring suit against WestPoint, and to discuss the possibility of their retaining him as counsel. Tr. 524-25, 571, 615, 651-2; *see also Allen*, 908 F. Supp. at 1216. By September 1989, each of the *Allen* Plaintiffs except John Currier ("Currier") and Gerard P. Mandry ("Mandry") had signed a retainer agreement with Krumme. Plaintiffs Currier and Mandry signed such agreements in March and May 1990, respectively. *See Allen*, 908 F. Supp. at 1216. On June 6, 1990, the *Allen* Plaintiffs filed suit.

E. *Attorneys' Fees*

When management recommended installing change in control provisions in various WestPoint benefit plans, it also recommended reimbursing participants for legal fees expended in enforcing their rights under the plan following a change in control. *See* Def. Ex. B. Pursuant to this recommendation, the

following fee-shifting language was included in the EPI Amendment:

> If at any time upon or after a Change of Control there should arise any dispute as to the validity, interpretation or application of any term [or] condition of this Agreement . . . Cluett agrees, upon written demand by an Executive, to provide sums sufficient to pay on a current basis (either directly or by reimbursing the Executive or his legal representative) the Executive's costs and reasonable attorneys' fees (including expenses of investigation and disbursements for the fees and expenses of experts, etc.) (a) incurred by the Executive in connection with any dispute or litigation, regardless of whether the Executive is the prevailing party, involving any provision of this Agreement, provided that the court in which such litigation is pursued determines, upon application of any party, that the Executive or his legal representative did not initiate frivolously such litigation . . . .

EPI Amendment, Joint Ex. 18 at 5.

III. *Conclusions of Law*

A. *Mutual Mistake*

As noted, the *Allen* Plaintiffs seek to rescind the releases on the ground that both they and WestPoint mistakenly believed that 9.3% was the proper discount rate for calculating lump sums under the EPI Amendment. As a general rule, "a contract is voidable under the equitable remedy of rescission if the

parties entered into the contract under a mutual mistake of fact which is substantial and existed at the time the contract was entered into." *Rekis v. Lake Minnewaska Mountain Houses, Inc.*, 573 N.Y.S.2d 331, 335 (3d Dep't 1991). However, rescission is not available as a matter of law; it is an equitable remedy that the Court may impose in its discretion, after weighing all the attendant facts and circumstances. *See Alden Auto Parts Warehouse, Inc. v. Dolphin Equip. Leasing Co.*, 682 F.2d 330, 333 (2d Cir. 1982) (request for rescission "is addressed to the equity powers of the court"); *Rudman v. Cowles Communications, Inc.*, 30 N.Y.2d 1, 13 (1972) ("plaintiffs are not entitled as a matter of law to rescission. Such relief, lying in equity, is a matter of discretion.").

The facts presented in this case do not justify rescission, which is a "drastic" and "extraordinary" remedy under New York law. *See Canfield v. Reynolds*, 631 F.2d 169, 178 (2d Cir. 1980); *In re Kim*, 15 B.R. 198, 200 (Bankr. S.D.N.Y. 1981). While the parties were mistaken as to the discount rate in effect when the releases were signed, the *Allen* Plaintiffs were experienced businessmen who knew that they were "releasing" WestPoint from any further obligation to them. By executing the releases, the *Allen* Plaintiffs amended and superseded their EPI Amendments, so that the parties' contracts now called for lump sum payments to be computed using the PBGC-based rate. *See Barnum v. Millbrook Care Ltd. Partnership*, 850 F. Supp. 1227, 1236 (S.D.N.Y.), *aff'd*, 43 F.3d 1458 (2d Cir. 1994) ("It is well established that a subsequent contract regarding the same matter will supersede the prior contract.").

The EPI Amendment was intended to give participants the actual present value of their benefits under the EPI Program. When WestPoint discovered that the Cluett Pension Plan's

outdated 5% rate applied to the EPI Amendment, it made a good-faith effort to correct this drafting mistake. The fact that seven years later this Court determined that WestPoint's efforts were ineffective under ERISA is not proper grounds for rescission. *See Anita Foundations, Inc. v. ILGWU Nat'l Retirement Fund*, 902 F.2d 185, 189-90 (2d Cir. 1990) ("a settlement payment, made when the law was uncertain, cannot be successfully attacked on the basis of any subsequent resolution of the uncertainty.").

Rescinding the releases would create an entirely unfair result: WestPoint would be forced to pay the *Allen* Plaintiffs nearly twice the market-based present value of their EPI benefits. *See* Def. Ex. I. Such an outcome would undermine the WestPoint Board's understandable desire to harmonize the payout methodologies used in its various benefit plans. Moreover, it would provide the *Allen* Plaintiffs with an undeserved and unintended windfall.[6]

Several of the *Allen* Plaintiffs testified that they did not seek a windfall, but only a fair approximation of the present value of their benefits under the EPI Program. Tr. 625, 656-7, 851-2, 866. I find that each of them has already received such payment and that rescinding the releases would only work an

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6. At trial, the *Allen* Plaintiffs presented evidence of specific benefits — such as a restricted stock plan — contained in some WestPoint plans that were not available under the EPI Program. Tr. 968. They suggested that the 5% discount rate may have been intended to compensate for such differences. However, there is absolutely no evidence that the inclusion of the 5% rate was anything other than a mistake. Moreover, it is not clear that the benefit plans available to WestPoint's executives were more generous than those provided to Cluett's executives; indeed, Roark, who worked for both companies, testified that the opposite was true. Tr. 1081, 1086.

injustice upon WestPoint. I therefore decline to impose the equitable remedy of rescission.

B. *Attorneys' Fees*

The attorneys' fee clause contained in the EPI Amendment is extremely broad. It provides costs and attorneys' fees to an executive for "any dispute as to the validity, interpretation or application of any term [or] condition of this Agreement . . . regardless of whether the Executive is the prevailing party." Joint Ex. 18. The only requirements are that the dispute arise "upon or after a change of control," and that the executive does not "frivolously" bring suit.

Defendants contend that the fee-shifting clause was only intended to apply to disputes with a hostile acquiror such as Farley, not disputes with WestPoint's prior management. However, on its face the clause does not distinguish between disputes with outgoing management and those with incoming management. Rather, it mandates that an executive be compensated for "*any* dispute" concerning the interpretation or application of any term of the EPI Amendment (provided the dispute arises upon or after a change in control, and is not frivolous). Where a contract's language is unambiguous, " 'its meaning must be determined from the four corners of the instrument without resort to extrinsic evidence of any nature.' " *Goodheart Clothing Co. v. Laura Goodman Enterprises, Inc.*, 962 F.2d 268, 272 (2d Cir. 1992) (quoting John D. Calamari & Joseph M. Perillo, *Contracts* 166-67 (3d ed. 1987)). I therefore reject Defendants' claim that the clause does not apply to disputes with WestPoint's old management.[7]

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7. Because it might well be the case that WestPoint did not intend for the attorneys' fee provision to apply to disputes with prior (Cont'd)

Appendix B

Neither the *Allen* action nor the *Krumme* action could reasonably be termed frivolous. An action is frivolous where it is "clear under existing precedents that there is no chance of success and no reasonable argument to extend, modify or reverse the law as it stands." *Mareno v. Rowe*, 910 F.2d 1043, 1047 (2d Cir.), *cert. denied*, 498 U.S. 1028 (1991). This is not the situation here, where both actions have involved hotly contested, close questions of law and fact. Accordingly, Plaintiffs are entitled to attorneys' fees if their disputes arose "upon or after a change in control."

1. *Allen Plaintiffs*

Under the EPI Amendment, a participant was not entitled to a lump sum payment unless and until a change in control actually occurred: "upon the occurrence of a Change in Control the Executive . . . shall be paid in a lump sum a benefit equal to the Actuarial Equivalent of the Executive's . . . Accrued Benefit . . . ." EPI Amendment, Joint Ex. 18 at 3. Prior to a change in control, the *Allen* Plaintiffs had no right to any lump sum payment, and no legally cognizable dispute with WestPoint.

The subject of the *Allen* Plaintiffs' lawsuit is their right to a lump sum payout calculated using a 5% discount rate. Their

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(Cont'd)

management, this result may seem unfair. However, the language of the provision is unambiguous, and the Court is not empowered to rewrite the terms of a contract. *See Breed v. Insurance Co. of North America*, 46 N.Y.2d 351, 355 (1978) (court should not "vary" contract to "accomplish its notions of abstract justice or moral obligation"); *Moshiko, Inc. v. Seiger & Smith, Inc.*, 529 N.Y.S.2d 284, 288 (1st Dep't), *aff'd*, 72 N.Y.2d 945 (1988) (court may not invent ambiguity where none exists).

dispute with WestPoint could not possibly have arisen until April 5, 1989, when the lump sums became due and they did not receive such a payout. The *Allen* Plaintiffs are therefore entitled to be compensated by WestPoint for their costs and attorneys' fees.[8]

2. *Krumme*

Unlike the *Allen* Plaintiffs, Krumme began fighting with WestPoint management over his EPI benefits prior to the Farley takeover. He wrote letters asserting that his benefit should be calculated using a 5% discount rate, and brought suit against WestPoint on March 24, 1989, approximately two weeks before a change in control occurred. Nonetheless, because Krumme's rights under the EPI Amendment could not have vested until April 5, 1989, his "dispute" — like that of the *Allen* Plaintiffs — could not have arisen until that time. WestPoint must therefore compensate Krumme for the costs and attorneys' fees he incurred in this suit.

IV. *Conclusion*

For the foregoing reasons, I decline to rescind the releases executed by the *Allen* Plaintiffs. Further, I find that both the *Allen* Plaintiffs and Krumme are entitled to have their attorneys' fees and costs paid by WestPoint.

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8. In actuality, most of the *Allen* Plaintiffs had no dispute with WestPoint until well after April 5, 1989. At trial, all but one of the *Allen* Plaintiffs testified that when they received their lump sum payouts, they believed they had been paid all to which they were entitled. Tr. 520-21, 570, 614, 648, 721, 847, 864, 880. Hence, their dispute did not really "arise" until the late summer of 1989, when Robert Krumme contacted them and encouraged them to file suit.

Appendix B

SO ORDERED:

Shira A. Scheindlin
U.S.D.J.

Dated: New York, New York
May 13, 1996

APPENDIX C — AMENDED OPINION AND ORDER OF THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK DATED FEBRUARY 10, 1997

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

90 Civ. 3841 (SAS)

GORDON E. ALLEN, JOHN CURRIER, JAMES J. DUNNE, LEO FORNERO, GERARD P. MANDRY, NORMAN K. MATHESON, BRUCE E. MOORE, NICHOLAS PALLOTTA and COCHRAN B. SUPPLEE,

Plaintiffs,

-against-

WESTPOINT-PEPPERELL, INC., D. MICHAEL ROARK, C. POWERS DORSETT and BARRY F. SHEA,

Defendants.

AMENDED OPINION AND ORDER

SHIRA A. SCHEINDLIN, U.S.D.J.:

This Opinion addresses plaintiffs' state common law claims for (1) constructive fraud, (2) negligent misrepresentation, and (3) fraudulent omission. Plaintiffs have submitted these claims for the Court's determination based on a bench trial held earlier this year to determine related issues. For the reasons set forth below, I find defendants[1] not liable with regard to plaintiffs' claims.

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1. Plaintiffs withdrew their claims against defendant Barry Shea by Stipulation of Discontinuance dated January 22, 1997.

Appendix C

Factual Background

Familiarity with the facts of this case will be presumed for the purposes of this opinion as they have been thoroughly discussed by this Court and the Second Circuit during the long course of this litigation. There is no need to recite them here. *See Allen v. WestPoint-Pepperell, Inc.*, 945 F.2d 40, 41-44 (2d Cir. 1991); *Allen v. WestPoint-Pepperell, Inc.*, 933 F. Supp. 261, 263-268 (S.D.N.Y. May 13, 1996); *Allen v. WestPoint-Pepperell, Inc.*, No. 90-3841, 1996 WL 2004, at *1-2 (S.D.N.Y. Jan. 3, 1996); *Allen v. WestPoint-Pepperell, Inc.*, 908 F. Supp. 1209, 1212-1217 (S.D.N.Y. 1995).

Procedural History

In an Opinion and Order dated November 2, 1995, I held the Cluett Committee had no authority under ERISA to change the discount rate contained in the Cluett Pension Plan. *See Allen v. WestPoint-Pepperell, Inc.*, 908 F. Supp. 1209, 1222 (S.D.N.Y. 1995). "Accordingly, the 5% discount rate printed in the Cluett Pension Plan was never validly changed and was at all relevant times one of the actuarial assumptions contained in the Cluett Pension Plan for purposes of the EPI Amendment." *Id.* at 1222-23.

On December 11, 1995, the parties agreed to litigate the change of control issue, the mutual mistake and rescission issues and the question of attorneys' fees before reaching the state common law claims now at issue. A bench trial was held to develop a record on which to resolve those issues. In a Memorandum Opinion dated January 3, 1996, I found that, for purposes of the EPI Amendment, a "change of control" occurred on April 5, 1989. In an Opinion and Order dated May 13, 1996,

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I declined to rescind the Releases signed by plaintiffs on the basis of mutual mistake and granted attorneys' fees to plaintiffs. *See Allen v. WestPoint-Pepperell, Inc.*, 933 F. Supp. 261 (S.D.N.Y. May 13, 1996).

Discussion

I. ERISA Preemption and Waiver of Preemption

A. ERISA Preemption

A threshold question in the instant action is whether ERISA's preemption clause bars plaintiffs from bringing state common law claims to enforce the EPI pension plan.[2] In pertinent part, ERISA's preemption clause provides as follows:

> Except as provided in subsection (b) of this section, the provisions of this subchapter and subchapter III of this chapter shall supersede any and all State laws insofar as they may now or hereafter relate to any employee benefit plan described in [ERISA § 4(a)] and not exempt under [ERISA § 4 (b)].

ERISA § 514(a), codified at 29 U.S.C. § 1144(a). The legislative history behind the preemption clause makes it clear that Congress intended to supplant all state regulation of

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2. The EPI plan is a "top-hat" plan that covered only upper-echelon management personnel. Nevertheless, it is subject to ERISA's preemption clause. *See Bigda v. Fischbach Corp.*, 898 F. Supp. 1004, 1015-16 (S.D.N.Y. 1995), *aff'd*, 1996 WL 107342 (2d Cir. 1996) (summary affirmation based on other grounds). *See also Barrowclough v. Kidder, Peabody & Co. Inc.*, 752 F.2d 923, 936-37 (3d Cir. 1985), *overruled in part on other grounds*, 7 F.3d 1110 (3d Cir. 1993).

employee benefit plans with a uniform federal system.[3] The United States Supreme Court has construed ERISA's preemption language as "deliberately expansive, and designed to establish pension plan regulation as exclusively a federal concern." *Pilot Life Ins. Co. v. Dedeaux*, 481 U.S. 41, 45-46 (1987) (quotations omitted). ERISA's preemption clause has also recently been described as "among the broadest that can be found in the law." *See Geller v. County Line Auto Sales, Inc.*, 86 F.3d 18, 22 (2d Cir. 1996). *See generally* James F. Jorden et al., *Handbook on ERISA Litigation* § 2.03 (1994) (describing the wide preemptive effect of ERISA on state law).

This Circuit has previously held that a common law fraud claim for misconduct arising from the administration of an ERISA plan may be preempted. In *Diduck v. Kaszycki & Sons Contractors, Inc.*, 974 F.2d 270 (2d Cir. 1992), a demolition company failed to make required pension fund contributions for a group of "off-the-books" workers. The Second Circuit held the plaintiffs' common law fraud claim on behalf of participants and beneficiaries of the pension plan was preempted on the ground that the claim had "as a critical factor in establishing liability the existence of a plan and duties similar to those imposed by ERISA." *Id.* at 288 (quotation omitted).

However, the rule of *Diduck* does not require the preemption of all common law claims arising out of ERISA

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3. U.S. Representative Dent, who sponsored ERISA in the House, stated: "Finally, I wish to take note of what is to many the crowning achievement of this legislation, the reservation to Federal authority the sole power to regulate the field of employee benefit plans. With the preemption of the field, we round out the protection afforded participants by eliminating the threat of conflicting and inconsistent State and local regulations." 120 Cong. Rec. 29197 (1974) (quoted in *Shaw v. Delta Air Lines, Inc.*, 463 U.S. 85, 99 (1983)).

plans. The intent of Congress in drafting ERISA's preemption clause "was not to foreclose every state action with a conceivable effect upon ERISA plans, but to maintain exclusive federal control over the regulation of such plans." *NYS Health Maintenance Org. Conference v. Curiale*, 64 F.3d 794, 803 (2d Cir. 1995). Holding that ERISA's preemption clause should not be read to contravene the statute's underlying purpose to protect the interests of participants and beneficiaries of employee benefit plans, the Second Circuit recently held that a state common law claim that "seeks to advance the rights and expectations created by ERISA is not preempted simply because it may have a tangential impact on employee benefit plans." *Geller*, 86 F.3d at 23. In *Geller*, the Second Circuit held that "the essence of the plaintiffs' fraud claim does not rely on the pension plan's operation or management" but rather on defendants' fraudulent misrepresentation of facts relating to a pension plan. *Id.* Where a fraud claim is presented within the context of a pension benefit plan, ERISA does not automatically preempt state common law actions. *Id.*

It is impossible to fit plaintiffs' claims within the *Geller* exception to ERISA preemption of state law actions. Here, plaintiffs' common law actions are brought to enforce the terms of the EPI agreement as they existed before plaintiffs signed Releases altering those terms in 1989. The gravamen of plaintiffs' remaining claims is that, in soliciting plaintiffs' signature on the Release forms, defendants' negligently misrepresented material facts, and fraudulently omitted other material facts, thus causing plaintiffs to sign the Releases to their detriment. Plaintiffs are seeking the amount of EPI benefits that they would have received before the Releases were signed. Understood as such, plaintiffs' claims cannot be classified as "tangential" to the EPI plan. Rather they must be seen as what

they are: an attempt to enforce the EPI plan under terms most favorable to plaintiffs. I therefore find that ERISA's preemption clause applies to the instant claims.

B. Waiver of ERISA Preemption

Both parties agree that ERISA's preemption clause is an affirmative defense that may be waived. Defendants agree to waive any such preemption defense. *See* Letter from Defendants to the Court, dated November 21, 1996; Letter from Plaintiffs to the Court, dated November 22, 1996. However, that the parties have agreed to the application of New York common law to resolve the instant claims does not end the inquiry into the question of preemption. The preemptive effect of federal legislation on state law implicates broad questions of federalism that cannot always be dismissed by the consent of litigating parties. *See, e.g., Florida Lime & Avocado Growers v. Paul*, 373 U.S. 132, 142 (1963) ("The test of whether both federal and state regulations may operate, or the state regulation must give way, is whether both regulations can be enforced without impairing the federal superintendence of the field, not whether they are aimed at similar or different objectives."); *Hines v. Davidowitz*, 312 U.S. 52, 67 (1941) (whether federal legislation preempts a state law turns on whether or not it "stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress."). *See generally* Laurence H. Tribe, *American Constitutional Law*, §§ 6-26, 6-27 (2d ed. 1988) (discussing federal limits on state power).

The language of ERISA itself does not directly address the question of whether the statute's preemptive effect may be waived. Thus courts have looked to ERISA's legislative history in an attempt to determine Congress's intent regarding this

issue. Defendants cite four Circuit decisions that have held ERISA preemption is an affirmative defense and may be waived.[4] *See Wolf v. Reliance Standard Life Ins. Co.*, 71 F.3d 444, 448-49 (1st Cir. 1995); *Dueringer v. General Am. Life Ins. Co.*, 842 F.2d 127, 130 (5th Cir. 1988); *Gilchrist v. Jim Slemons Imports, Inc.*, 803 F.2d 1488, 1497 (9th Cir. 1986); *Rehabilitation Inst. of Pittsburgh v. Equitable Life Assur. Soc'y*, 131 F.R.D. 99, 101 (W.D. Pa. 1990), *aff'd*, 937 F.2d 598 (3d Cir. 1991) (affirmed without opinion). These cases hold that ERISA's preemption clause is a choice of law provision, rather than a choice of forum provision.[5]

Wolf's holding that the protection of ERISA's preemption clause is waivable was in part grounded in the First Circuit's determination that:

> [T]he interests in uniformity which Congress hoped to serve in ERISA did not extend to permitting defendant corporations, often more sophisticated about ERISA than individual plaintiffs, to sit on their hands and not claim the [preemption] defense until the last minute. That employers were meant to enjoy the benefits of uniformity did not mean that they could not forego those benefits.

Wolf, 71 F.3d at 448 (citations omitted). *Wolf* is also based on precedent. In *Pilot Life Ins. Co. v. Dedeaux*, 481 U.S. 41, 44-

4. The question of whether ERISA preemption is jurisdictional and thus not waivable, or an affirmative defense that may be waived, has not been addressed by the Second Circuit.

5. It is well established that choice of forum preemption is not waivable. *See Int'l Longshoremen's Ass'n v. Davis*, 476 U.S. 380, 398-99 (1986).

46 (1987), the Supreme Court concluded that ERISA's preemption clause was modeled after the preemption clause of the Labor Management Relations Act ("LMRA") and that courts should look to LMRA preemption decisions when deciding the scope of ERISA's preemption clause. *Wolf*, observing that the First Circuit previously held that LMRA preemption is waivable in *Sweeny v. Westvaco Co.*, 926 F.2d 29, 40 (1st Cir.) (Breyer, C.J.), *cert. denied*, 502 U.S. 899 (1991), determined, *a fortiori*, that ERISA preemption was waivable.

The Second Circuit has not ruled directly on the issue of whether LMRA preemption is waivable. However, Chief Judge (now Justice) Breyer's analysis in *Sweeney* is both thorough and persuasive. In fact, *Sweeney's* holding that LMRA preemption is waivable is in part based on the Fifth and Ninth Circuits' holdings that ERISA preemption is waivable. *Id.* at 40 (citing *Dueringer*, 842 F.2d at 130 and *Gilchrist*, 803 F.2d at 1497). These cases lead me to conclude that ERISA's preemption clause was intended as a choice of law provision. Thus understood, it cannot be interpreted to be jurisdictional and non-waivable and defendants may effectively waive their right to raise ERISA's preemption clause in opposition to plaintiffs' state law claims.

II. Legal Standards Applicable to Plaintiffs' State Common Law Claims

A. Elements of Plaintiffs' Common Law Actions

Plaintiffs now bring three common law actions against defendants for (1) constructive fraud, (2) negligent misrepresentation and (3) fraudulent omission. Set forth below is a brief summary of the required elements of each action under the common law of New York.

Appendix C

Under New York law, constructive fraud may be defined as "a breach of duty which, irrespective of moral guilt and intent, the law declares fraudulent because of its tendency to deceive, to violate a confidence or to injure public or private interests which the law deems worthy of special attention." *Grand Union Mount Kisco Emp. Fed. Cr. U. v. Kanaryk*, 848 F. Supp. 446, 455 (S.D.N.Y. 1994) (quoting *Brown v. Lockwood*, 432 N.Y.S.2d 186, 193 (2d Dep't 1980)). To establish a claim for constructive fraud, plaintiffs must show (1) a confidential or fiduciary relationship[6] exists, or alternatively that one party has superior knowledge not available to the other; (2) a representation of fact which is false; (3) justifiable reliance on such false representation; and (4) detriment as a result of such reliance. *See Callahan*, 514 N.Y.S.2d at 821 (citations omitted). A plaintiff who attempts to establish a *prima facie* case for constructive fraud by establishing the abuse of a fiduciary or confidential relationship need not prove actual knowledge of falsity or scienter. *Id.* (citing, *inter alia*, *Del Vecchio v. Nassau County*, 499 N.Y.S.2d 765, 768 (2d Dep't 1986); *Brown*, 432 N.Y.S.2d at 193; 24 N.Y. Jur., Fraud and Deceit §§ 2, 17, 109 (1962)).

The elements of negligent misrepresentation are (1) carelessness in imparting words; (2) upon which others were expected to rely; (3) upon which they did justifiably rely; (4) to their detriment; and (5) the author must express the words directly, with knowledge they will be acted upon, to one whom the author is bound by some relation or duty of care. *See Ultramares Corp. v. Touche, Nevin, & Co.*, 255 N.Y. 170 (1931)

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6. *Brown*, 432 N.Y.S.2d at 194, further defined the required relationship as one "warranting the trusting party to repose his confidence in the defendant and therefore to relax the care and vigilance that he would ordinarily exercise in the circumstances."

(Cardozo, J.); *Glanzer v. Shepard*, 233 N.Y. 236, 239-241 (1922) (Cardozo, J.); *Mallis v. Bankers Trust Co.*, 615 F.2d 68, 81-82 (2d Cir. 1980) (Friendly, J.), *cert. denied*, 449 U.S. 1123 (1981). *See also Patell Industrial Machine v. Toyoda Machinery U.S.A.*, 880 F. Supp. 96, 99 (N.D.N.Y. 1995) (citing, *inter alia*, *Mallis*, 615 F.2d at 81).

New York also recognizes a claim for fraudulent omission. This action is a permutation of the common law action for fraud. As one New York court explained, "nondisclosure is tantamount to an affirmative misrepresentation where a party to a transaction is duty-bound to disclose certain pertinent information." *Callahan v. Callahan*, 514 N.Y.S.2d 819, 821 (3d Dep't 1987). To establish a claim for failure to disclose material information, plaintiffs must show (1) plaintiffs and defendants were party to a contract; (2) defendants had superior knowledge of material facts; (2) that knowledge was not available to plaintiffs; (3) defendants failed to disclose that knowledge to plaintiffs; (4) scienter[7]; (5) that plaintiffs were justifiably deceived by that failure to disclose; and that (6) plaintiffs were damaged as a result of the failure to disclose. *See Allen v. WestPoint-Pepperell, Inc.*, 945 F.2d 40, 45-46 (2d Cir. 1991); *Callahan*, 514 N.Y.S.2d at 821; *Young v. Keith*, 492 N.Y.S.2d 489, 490-91 (3d Dep't 1985).

B. Standards of Proof

It is commonly accepted under New York law that "evidence of fraud is rarely susceptible of direct proof and must ordinarily be established by circumstantial evidence and the

7. The scienter requirement of fraud actions may be satisfied by a showing of "reckless indifference to error". *Skrine v. Staiman*, 292 N.Y.S.2d 275, 276 (2d Dep't 1968), *aff'd*, 298 N.Y.S.2d 727 (1969).

legitimate inferences arising therefrom." *Kanaryk*, 848 F. Supp. at 455. *See also Goshen Litho, Inc. v. Kohls*, 582 F. Supp. 1561, 1564 (S.D.N.Y. 1983); *Abrahami v. UPC Const. Co., Inc.*, 638 N.Y.S.2d 11, 13 (1st Dep't 1996). Recognizing the ease with which such inferences may be asserted, New York courts require fraud and constructive fraud to be proven by clear and convincing evidence. *See Katara v. D.E. Jones Commodities, Inc.*, 835 F.2d 966, 971 (2d Cir. 1987); *Kanaryk*, 848 F. Supp. at 455; *Geller v. National Westminster Bank, USA*, 770 F. Supp. 210, 212-13 (S.D.N.Y. 1991). This evidentiary standard forbids the awarding of relief "whenever the evidence is loose, equivocal or contradictory". *Abrahami*, 638 N.Y.S.2d at 13 (quotation omitted).

Negligent misrepresentation is a species of fraud that replaces the required showing of scienter with a showing of negligence. Like actions for fraud, negligent misrepresentation actions typically are based on inference rather than direct evidence. Thus, New York's high standard of "clear and convincing" proof applies to actions for negligent misrepresentation as well as actions for intentional fraud. *See Alice D. v. William M.*, 450 N.Y.S.2d 350, 354 (N.Y. City Civ. Ct. 1982). *Cf. Ajax Hardware Mfg. Corp. v. Industrial Plants Corp.*, 569 F.2d 181, 186 (2d Cir. 1977) (discussing "clear and convincing" standard required of actions for fraud and citing *Jo Ann Homes at Bellmore, Inc. v. Dworetz*, 302 N.Y.S.2d 799 (1969); *Manchel v. Kasdan*, 144 N.Y.S.2d 694 (1st Dep't 1955) (*per curiam*), *aff'd*, 151 N.Y.S.2d 940 (1956); *Cave v. Green*, 120 N.Y.S.2d 865 (1st Dep't 1953), *aff'd*, 308 N.Y. 754 (1955)). Similarly, an action for fraudulent omission is a kind of fraud action, *see Young*, 492 N.Y.S.2d at 490-91 (citing 24 N.Y. Jur. Fraud and Deceit § 106, at 159 (1962)), and requires plaintiffs to meet a "clear and convincing evidence" standard of proof.

Appendix C

III. Determination of Plaintiffs' Claims

A. Plaintiffs' Allegations

All three of plaintiffs' common law claims arise out of the same set of factual allegations of defendants' wrongdoing, which are briefly summarized here. In the mid-1970's, Cluett Peabody & Co. ("Cluett") agreed with its senior executives to institute an Executive Permanent Insurance Program (the "EPI Program"), under which deferred compensation benefits would be paid to the senior executives.[8] WestPoint-Pepperell, Inc. acquired Cluett in January, 1986. In anticipation of a hostile takeover during November, 1988, WestPoint offered the EPI Program participants the opportunity to subscribe to a favorable change in terms of the agreement, sending each participant an amendment form (the "EPI Amendment"). Each of the plaintiffs signed and returned that form. Under the EPI Amendment, a participant would be entitled to receive from WestPoint lump sum payments in an amount equal to the "actuarial equivalent" of the participant's retirement benefits in the event of a takeover.

The EPI Amendment defined "actuarial equivalent" as an amount having "the same present value as the accrued benefit". To calculate the actuarial equivalent, the EPI Amendment referred to "the actuarial assumptions contained in Cluett's Employee Retirement Plan." That Plan provided:

> "Actuarial equivalent" means an amount of equal value when computed on the basis of interest,

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8. Under the EPI Program, each participant would be entitled to receive 30% of his final base salary for life upon reaching the age of 65, with payments of half that amount made to a designated beneficiary upon the participant's death. *See Allen*, 945 F.2d at 41.

> mortality and other tables as shall be adopted from time to time by the [Cluett Pension] Committee on the advice of the Actuary, the current factors being as specified below:
>
> (1) Mortality table. The . . . 1971 Group Annuity Mortality Table projected to 1978.
>
> (2) Interest rate. 5% per annum, compounded annually.

See Allen, 945 F.2d at 42.[9]

Plaintiffs allege that in early 1989, defendants' interest in participating in a leveraged buy-out of WestPoint motivated

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9. The process of determining the present value of a future cash flow is often referred to as "discounting" or "capitalizing" an income stream. The most simple formula for approximating the present value of a cash flow one year from now may be expressed:

$$PV = C / (1 + R)$$

PV equals the present value of the future income, C is the amount of the income expected one year from now, and R is the annual rate of interest on C amount of money invested now. *See* R. Brealey & S. Myers, Principles of Corporate Finance 29-31 (4th ed. 1991) (explaining how to determine the value of assets that produce future income); Michael C. Thomsett, The Mathematics of Investing 30-31 (1989) (same).

As R *decreases*, the present value of the future income *increases*. Applying this principle to the instant case, one sees that as the discount rate decreases, the present value of the benefits owed to EPI participants increases. It is for this reason that plaintiffs seek to apply an interest rate of 5% and defendants argue that the applicable interest rate is 9.3%.

them to execute "drastic cost-cutting measures". *See* Plaintiffs' Trial Memorandum at 7. It was at this time that WestPoint's management attempted to reduce the EPI payments by increasing the interest rate to 9.3%, thereby saving WestPoint approximately $4 million dollars. Plaintiffs now maintain "[b]ecause of the serious conflict of interest these events created for WestPoint's executives, they should have exercised extreme care both in addressing the discount rate issue and in communicating with the EPI Participants." *Id.*

Plaintiffs base their common law actions on the combination of the Releases and the February 22 Letter. The February 22 Letter, addressed from defendant Roark to plaintiff Allen, states in pertinent part:

> There has apparently been some confusion as to the method of calculation to be employed in determining the lump sum benefit under the Cluett Deferred Compensation Agreements. Some participants have told us that they were led to believe that a 5% discount rate would be used to determine lump sum values. This is incorrect . . . . The [discount rate] is 9.3%. Because of the confusion regarding the discount rate, we are giving you an opportunity to revoke the amendment and are enclosing an election form to revoke the [EPI Amendment] and are enclosing an election form which is to be used to affirm or revoke the [EPI Amendment].

See Affidavit of Frederick A. Brodie, Counsel for defendants, at Exhibit 2. The Releases gave plaintiffs the choice of ratifying the 9.3% rate or revoking the EPI Amendment altogether. The former would allow plaintiffs to receive a lump sum payout

upon the event of a takeover, but a smaller payout than would have been received if the 5% interest rate was used. The latter would prevent plaintiffs from receiving any lump sum payout upon the event of takeover; if plaintiffs revoked the EPI Amendment they would not begin to receive any payouts of benefits under the EPI Program until age 65.

Plaintiffs argue that "the February 22 Letter misrepresented the applicable interest rate and failed to advise the EPI participants of material information regarding the timing and manner in which WestPoint had purported to reduce the lump sum payouts." Plaintiffs' Trial Memorandum at 2. Plaintiffs claim WestPoint solicited the Releases solely through the February 22 Letter, which "at best was an effort to slide the 9.3% discount rate by the EPI Participants without making too many waves and to gather a parcel of Releases in the bargain." *Id.* at 8.

B. Claim for Constructive Fraud

Plaintiffs' action for constructive fraud fails because plaintiffs have not shown by clear and convincing evidence that defendants made a false representation of fact upon which they relied to their detriment. Plaintiffs assert that the February 22 Letter's representation that the applicable interest rate was 9.3%, as opposed to 5%, was false because the Cluett Committee lacked the authority to change that rate. *See* Plaintiffs' Trial Memorandum at 5. Plaintiffs also claim that defendant Dorsett made a false representation of fact on February 16, 1989 when he stated to Robert Krumme that the 5% interest rate had never been used to calculate a participant's benefits and that subsequently defendant WestPoint made false statements of fact to support Dorsett's statement. *See* Plaintiffs' Trial Memorandum at 9-11.

Neither of these arguments will sustain a claim of constructive fraud. The February 22 Letter makes no false representation. It states that the 9.3% rate had been adopted for all WestPoint retirement benefit plans. Because the Cluett Committee had indeed adopted the 9.3% rate, that statement was true at the time it was made. Plaintiffs, of course, argue that defendants knew at the time that the Committee lacked the power to make this change. However, the record indicates that WestPoint management believed that if the Plan Actuary agreed that the 5% discount rate was outdated, unfair, and inconsistent with WestPoint's other pension plans, the Cluett Committee could adopt the 9.3% rate.[10] *See Allen*, 933 F. Supp. at 266 (finding that WestPoint management believed the Cluett Committee had the authority to adopt the 9.3% rate).

Similarly, neither Dorsett's alleged statement that the 5% rate had never been used to calculate a participant's benefits, nor WestPoint's allegedly false documentary support of that statement will sustain the constructive fraud claim. Whether or not these representations were false, there is no clear and convincing evidence that plaintiffs relied on them to their detriment. There is no evidence that Krumme informed plaintiffs of his interaction with Dorsett, or that Krumme informed plaintiffs of WestPoint's subsequent attempts to substantiate Dorsett's statement, before plaintiffs signed their respective Releases. In fact, plaintiffs' testimony at trial indicates that they did not even speak with Krumme before signing the Releases. Tr. at 514-517 (Allen); 605 (Moore); 646-48 (Mandry); 716-718 (Fornero); 842-45 (Pallotta); 860-61

10. Although I invalidated the Cluett Committee's attempt to change that rate over six years later, this does not retroactively transform the February 22 Letter into a false representation of fact upon which plaintiffs may rest an action for constructive fraud.

(Matheson); 877-78 (Currier).[11] If plaintiffs did not rely on Dorsett's assertion and WestPoint's subsequent documentary support of that assertion in deciding whether to ratify the 9.3% rate, no claim for constructive fraud will lie.

C. Negligent Misrepresentation

To succeed on their negligent misrepresentation claim, plaintiffs must first establish that the February 22 Letter and Releases constitute "carelessness in imparting words". *See* Part II(A). Plaintiffs argue that the February 22 Letter and Releases together failed to inform them clearly (1) that the rate incorporated into the original EPI Amendment had, mistakenly or not, been 5%; (2) of the Cluett Committee's decision to change the interest rate to 9.3%; (3) of the defendants' potential conflict of interest stemming from their efforts to reduce costs in order to participate in a leveraged buy-out of WestPoint; (4) that the change of interest rate would reduce the amount of benefits that plaintiffs would receive on change of ownership; and (5) that plaintiffs had the option of challenging the 9.3% rate without forfeiting their right to a lump-sum payout upon change of control. *See* Plaintiffs' Trial Memorandum at 3-7, 11-12. Thus, plaintiffs' negligent misrepresentation claim rests as much on what defendants failed to disclose as it rests on what defendants actually said.[12]

Despite these arguments, I conclude that the combined effect of the February 22 Letter and the Releases did not

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11. Dunne did not testify at trial.

12. An action for negligent misrepresentation may be based on the omission of material information: "half of the truth may obviously amount to a lie, if it is understood to be the whole." *Prosser and Keeton on the Law of Torts* § 106 at 738 (5th ed. 1984).

constitute a negligent misrepresentation on the part of defendants. It was not misrepresentative to fail to inform plaintiffs that the applicable discount rate had always been 5%. The record indicates that defendants believed at all times that the EPI Amendment was intended to incorporate a 9.3% rate — which is to say, a discount rate that would cause the participants to receive the actual present value of their EPI benefits. *See Allen*, 933 F. Supp. at 269. Defendants have consistently maintained that the inclusion of the 5% discount rate by reference to the Cluett Pension Plan was a mistake. *See* Defendants' Trial Memorandum at 9-10. Thus, defendants' statements that the applicable discount rate was 9.3% was based on defendants' understanding of the EPI Agreement, and cannot be viewed as a misrepresentation.

Nor was it a misrepresentation to fail to explicitly inform plaintiffs that the 9.3% discount rate would reduce the amount of benefits EPI participants would receive upon a change of control, or that they had the option of challenging the 9.3% rate without forfeiting their right to a lump-sum payout. Plaintiffs are all sophisticated businessmen. As such, they are obliged under New York law to exercise ordinary diligence and to conduct an independent appraisal of their choices before entering into any business or legal transactions. *See Abrahami*, 638 N.Y.S.2d at 14. If plaintiffs did not understand the financial consequences of accepting the 9.3% rate, they should have sought the advice of an independent attorney or accountant before signing the Releases.

Additionally, defendants had no obligation to disclose the Cluett Committee's decision to "change" the discount rate to 9.3%. The record indicates that the Cluett Committee attempted to conform the relevant documents to the parties' original

understanding regarding the discount rate to be used by the EPI Amendment. *See, e.g.*, Tr. at 913, 927-28 (Dorsett); Tr. at 1065-68 (Roark). As plaintiffs had already approved of the 9.3% rate when they signed the EPI Amendment, it is not reasonable to assume that knowledge of the Committee's action would have changed their decision to sign the Releases.

Nor were defendants obliged to inform plaintiffs of the possibility of a conflict of interest stemming from defendants' potential interest in a leveraged buy-out effort.[13] Plaintiffs allegation that defendants had a conflict of interest is not supported by "clear and convincing evidence". In theory, it is true that reducing WestPoint's outstanding expenses would make a leveraged buy-out more feasible by lowering the company's interest expense on any borrowed capital. Yet defendants have testified that they did not expect to derive any personal benefit from adopting the 9.3% discount rate. *See* Affidavit of Frederick Brodie, Counsel for Defendants, Ex. 4 at 132 (Deposition of D. Michael Roark) ("Q: At the time when you decided that the EPI discount rate should be changed, did you have any idea of the order of magnitude of so-called savings from making the change? A: No . . . . Q: Did you gain anything in the change in the EPI discount rate? A: No."); *Id.*, Ex. 19 at 94-95 (Deposition of C. Powers Dorsett) ("Q: Mr. Dorsett, do you have any personal motive in any action you took with respect to changes in the EPI discount rate? A: No."). Plaintiffs

13. Plaintiffs argue that WestPoint executives believed the success of a leveraged buy-out by a financial group with which they could participate depended on "drastic cost cutting measures." Plaintiffs' Trial Memorandum at 7. Plaintiffs base their conflict of interest argument on the allegation that defendants deliberately adopted the 9.3% discount rate in an effort to cut costs and thereby effectuate a leveraged buy-out. *Id.*

have produced no evidence that casts doubt on the veracity of this testimony.

Additionally, Dorsett testified that no definite prospect of a management buy-out existed after February 1, 1989. *See id.*, Ex. 19 at 96. While it may be true that WestPoint's Board of Directors continued to search for a friendly buyer after that date, the evidence suggests that no concrete possibility of a leveraged buy-out existed by February 16, 1989, when the Cluett Committee adopted the 9.3% rate. *See* Affidavit of Robert J. Hausen, Counsel for Plaintiffs, Ex. I at A000219 (indicating that as of February 16, 1989, WestPoint Board of Directors anticipated that Merrill Lynch Capital Partners and the Wasserstein Perella/Blackstone Group would make a friendly tender offer, but also stating that "no agreements had been reached" at that point). *See also* Letter from Robert J. Hausen, Counsel for Plaintiffs, to Court, dated January 24, 1997 at 2-3 (setting forth chronology of WestPoint's contact with prospective bidders). I therefore find there was no actual leveraged buy-out under way after February 1, 1989, and conclude that defendants cannot be said to have had a conflict of interest merely because they were looking for a "white knight" that would acquire WestPoint and save their jobs. Accordingly, defendants had no obligation to inform plaintiffs that they had a potential conflict of interest.

D. Fraudulent Omission

The scienter requirement of a claim for fraudulent omission is equivalent to the scienter requirement for all common law fraud actions. *See Skrine*, 292 N.Y.S.2d at 276 (citing *Ochs v. Woods*, 221 N.Y. 335 (1917); *Smith v. Hedges*, 223 N.Y. 176, 184 (1918); *Reno v. Bull*, 226 N.Y. 546 (1919)). Plaintiffs may

satisfy the scienter requirement of their fraudulent omission by a showing of "reckless indifference to error" or "a pretense of exact knowledge". *Id.* (quotations and citations omitted). Thus to succeed on a claim for fraudulent omission, plaintiffs must show by clear and convincing evidence that defendants were more than negligent in their failure to disclose material facts. *See Duggan v. Dep't of Motor Vehicles*, 295 N.Y.S.2d 706, 708-09 (1st Dep't 1968); *see also* Black's Law Dictionary 1271 (6th ed. 1990) ("Recklessness is a stronger term than mere or ordinary negligence"). Plaintiffs can succeed on their fraudulent omission claim only by showing that defendants knowingly or recklessly disregarded the risk of omitting material facts. The trial record does not support such a finding. There is no indication that defendants knowingly omitted material facts from either the February 22 Letter or the Releases. Nor is there clear and convincing evidence that defendants recklessly disregarded the risk that these two documents omitted material facts. Defendants are therefore not liable for fraudulent omission.

IV. Res Judicata and the Preclusive Effect of the Releases

I address defendants' res judicata arguments in order to provide a fully adjudicated trial record from which the parties may appeal.

A. Preclusive Effect of Releases

Defendants maintain that the Releases this Court previously declined to rescind bar plaintiffs' instant claims. *See* Defendants' Trial Memorandum at 5 ("By accepting a 9.3%. rate and releasing their claims under the EPI Program, the plaintiffs gave up any claim to a 5% rate."). This argument

misses the mark. Under New York law, a contract induced by misrepresentation or fraud is void. *See Gilbert v. Rothschild*, 280 N.Y. 66, 71 (1939). The contract itself, be it a Release or an amendment, cannot bar an action based on misrepresentation or fraud. *See Aaron Ferer & Sons Ltd. v. Chase Manhattan Bank*, 731 F.2d 112, 123 (2d Cir. 1984). *See generally* Dan B. Dobbs, *Law of Remedies* § 9.1 at 544-545 (describing torts of negligent misrepresentation and fraud arising out of contracts); Restatement (Second) of Torts § 549 (damages for fraudulent misrepresentation).

Nor are plaintiffs' present claims for damages barred by their previous rescission claim. It is settled law in New York that a party who was induced by misrepresentations to execute a contract of Release has three remedies from which to choose: (1) he may rescind the contract and sue in an action at law; (2) he may bring an equitable action to rescind the contract and in that action obtain full relief; and (3) he may retain what he has received under the fraudulent contract and bring an action at law to recover the damages sustained. *See Goldsmith v. National Container Corp.*, 287 N.Y. 438, 442-443 (1942). *See also duPont v. Perot*, 59 F.R.D. 404, 410 (S.D.N.Y. 1973) (following and quoting *Goldsmith*). Under New York law, a party may pursue simultaneous actions for fraud, misrepresentation and rescission. *See* N.Y. Civ. Prac. L. & R. § 3002(e) (McKinney 1996).

B. Defendants' Res Judicata Arguments

1. Claim Preclusion by Res Judicata or Law of the Case

Defendants contend that the doctrines of res judicata and the law of the case bar plaintiffs from relitigating the instant

claims. *See* Defendants' Trial Memorandum at 1-4 (citing *Woods v. Dunlop Tire Corp.*, 972 F.2d 36, 38 (2d Cir. 1992) (doctrine of claim preclusion bars all attempts to litigate issues that were or could have been litigated at a prior proceeding), *cert. denied*, 506 U.S. 1053 (1993)). These arguments are without merit as plaintiffs have always been prepared to litigate all their claims at one time. It was the defendants who requested that plaintiffs' claims be tried in two separate proceedings.

On December 11, 1995, the parties held a conference before the Court to discuss the unusual posture of this long-running case as it stood at that time. During that conference, Mr. Carling, Defendants' counsel, requested that the Court adjudicate the change of control issue, the mutual mistake issue and the question of attorneys' fees in a separate proceeding before reaching the instant misrepresentation issues. Mr. Carling stated two primary reasons for his request. First, his clients preferred to avoid the publicity of trial: "To avoid that spectacle of [defendants] being tried for fraud, the general counsel of [a] major public company being tried for fraud in front of a jury, we would like to see if it can be avoided by having the equitable trial first." Second, Mr. Carling stated that he believed proceeding in that manner would maximize the possibility of settlement. Transcript of December 11, 1995 Conference at 22-30.

I granted that request based on Mr. Carling's suggestion that such a bifurcation of the plaintiffs' case would increase the chances that the parties would settle their differences without resort to further litigation. It would be fundamentally unjust to allow defendants to defeat plaintiffs' claims now by raising res judicata and law of the case arguments. Despite defendants' arguments, nothing requires the Court to apply these

doctrines to bar plaintiffs' fraud claims. *See Federated Dept. Stores, Inc. v. Moitie*, 452 U.S. 394, 401 (1981) (doctrine of res judicata is not a technical rule, but rather a rule of fundamental and substantial justice); *In re PCH Assocs.*, 949 F.2d 585, 592 (2d Cir. 1991) (law of the case doctrine is a rule of practice and not a limit on judicial authority). *See generally* 1B James W. Moore, Moore's Federal Practice ¶¶ 0.404[1], 0.405[1] (2d ed. 1996) (discussing function and underlying policies of res judicata and law of the case doctrines).

2. Collateral Estoppel or "Issue Preclusion"

The doctrine of collateral estoppel (also known as "issue preclusion") provides that when an action between two parties terminates in a valid judgment, a later action between the parties may be affected even though it involves a different claim. *See Levy v. Kosher Overseers Association of America, Inc.*, No. 96-7051, 103, 1997 WL 7687, at *3 (2d Cir. Jan. 9, 1997) (*citing Parklane Hosiery Co., Inc. v. Shore*, 439 U.S. 322, 326 (1979)). *See generally*, Eli J. Richardson, *Taking Issue with Preclusion: Reinventing Collateral Estoppel*, 65 Miss. L.J. 41, 44-53 (1995) (discussing the background and purpose of collateral estoppel law). As a result, findings of fact from prior proceedings in this case must apply to the resolution of plaintiffs' instant claims if (1) the facts of the prior proceeding and the instant proceeding are identical; (2) the findings of fact were actually litigated and decided in a prior proceeding; (3) there was a full and fair opportunity for litigation in the prior proceeding; (4) the fact was necessary to support a valid and final judgment on the merits. *See id.* Defendants argue that such findings of fact bar plaintiffs from bringing their instant claims. *See* Defendants' Trial Memorandum at 1-2; *see also* Oral Arg. Tr. at 23-24.

Specifically, defendants argue that the factual issues of whether defendants acted in good faith in attempting to change the discount rate, and whether plaintiffs suffered any harm as a result of the Releases, have already been adjudicated. *See* Oral Arg. Tr. at 24. Defendants rely on the following portion of the May 13 Opinion to support their collateral estoppel claim:

> The EPI Amendment was intended to give participants the actual present value of their benefits under the EPI Program. *When WestPoint discovered that the Cluett Pension Plan's outdated 5% rate applied to the EPI Amendment, it made a good-faith effort to correct this drafting mistake.* The fact that seven years later this Court determined that WestPoint's efforts were ineffective under ERISA is not proper grounds for rescission. . . . Rescinding the releases would create an entirely unfair result: WestPoint would be forced to pay the *Allen* Plaintiffs nearly twice the market-based present value of their EPI benefits. See Def. Ex. I. Such an outcome would undermine the WestPoint Board's understandable desire to harmonize the payout methodologies used in its various benefit plans. *Moreover, it would provide the Allen Plaintiffs with an undeserved and unintended windfall.*

See Allen, 933 F. Supp. at 268-69 (underlining added; italics in original).[14] If this Court has found that plaintiffs were not

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14. The May 13 Opinion went on to state in a footnote: "At trial, the *Allen* Plaintiffs presented evidence of specific benefits — such as a restricted stock plan — contained in some WestPoint plans that were not available under the EPI Program. Tr. 968. They suggested that the

(Cont'd)

harmed by signing the Releases, that finding collaterally estops plaintiffs from bringing the instant common law claims: if plaintiffs cannot establish that they suffered harm as a result of signing the Releases, they have no viable common law claim."[15]

The question of whether plaintiffs suffered a legally cognizable injury as a result of defendants' conduct must be determined within the context of the contractual relationship between the parties. It would appear at first blush that a fraudulently induced Release that reduced the dollar amount received by plaintiffs upon a change of control constitutes a legally cognizable "harm" sufficient to establish a *prima facie* case for constructive fraud, negligent misrepresentation or fraudulent omission. However, as noted above, the May 13 Opinion explicitly found that the EPI Amendment was intended to provide participants with the actual present value of their benefits under the EPI Program. The May 13 Opinion also found

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(Cont'd)

5% discount rate may have been intended to compensate for such differences. However, there is absolutely no evidence that the inclusion of the 5% rate was anything other than a mistake. Moreover, it is not clear that the benefit plans available to WestPoint's executives were more generous than those provided to Cluett's executives; indeed, Roark, who worked for both companies, testified that the opposite was true. Tr. 1081, 1086." *Allen*, 933 F. Supp. at 269 n.6.

15. Each of plaintiffs' common law claims requires plaintiffs to establish that they relied on defendants' allegedly fraudulent or misrepresentative statements or omissions *to plaintiffs' detriment*. Plaintiffs attempt to satisfy this element by showing that they signed the Releases as a result of defendants' misrepresentations and omissions, and that in turn by signing the Releases plaintiffs lowered the amount of EPI Benefits to which they were entitled upon a change of control. See Part III(A), *infra*.

that using a 5% discount rate would have forced WestPoint to pay plaintiffs nearly twice the market-based present value of their EPI benefits. *See Allen*, 933 F. Supp. at 268. I therefore held that using a 5% discount rate would be "an undeserved and unintended windfall." *Id.* Thus, plaintiffs were not harmed by use of the 9.3% discount rate because that rate satisfied the original intent of the parties — to provide EPI participants with the actual present value of their benefits upon a change of control.

This finding collaterally estops plaintiffs from asserting that they suffered a legally cognizable harm as a result of signing the Releases. The first three prongs of the collateral estoppel test are easily satisfied. First, plaintiffs' instant claims arise out of the same operative facts upon which they brought their action for rescission. Second, this issue has been actually litigated and decided. Third, there can be no question that plaintiffs have had a full and fair opportunity to litigate this issue at the prior proceeding — indeed plaintiffs do not assert otherwise. The only remaining requirement, therefore, is that the finding was necessary to support the judgment on the merits of the rescission claim. The finding that plaintiffs were not harmed by the implementation of the 9.3% discount rate led directly to my conclusion that "[t]he facts presented in this case do not justify rescission, which is a 'drastic' and 'extraordinary' remedy under New York law." *Allen*, 933 F. Supp. at 268. Accordingly, plaintiffs are collaterally estopped from bringing their common law claims because they may not assert that they were harmed by signing the Releases.

Defendants also argue that the May 13 finding that defendants acted in "good faith" in attempting to change the discount rate precludes plaintiffs from asserting here that they

negligently misrepresented material facts. "Good faith" is admittedly an ambiguous term that has been defined to mean, among other things, "an honest belief, the absence of malice and the absence of design to defraud or to seek unconscionable advantage". *Black's Law Dictionary* 693 (6th ed. 1990). Using this definition, it follows that one could act both "in good faith" and "negligently". Furthermore, this May 13 *dicta* did not constitute a ruling on whether the February 22 Letter and Releases constituted a negligent misrepresentation. Because the May 13 Opinion does not clearly find that defendants' "good-faith effort to correct its drafting mistake" included a reasonably diligent effort to inform plaintiffs of all material facts, defendants cannot successfully rely on it to collaterally estop plaintiffs from asserting that defendants acted negligently.

V. Attorneys' Fees

The May 13 Opinion determined that plaintiffs are "entitled to be compensated by WestPoint for their costs and attorneys' fees". *Allen*, 933 F. Supp at 270. However, in light of the extraordinary amount of judicial resources already consumed by this litigation, it makes no sense to calculate the exact amount of attorneys' fees owed at this stage. Defendant WestPoint has announced its intention to challenge this Court's determination that it must pay plaintiffs' attorneys' fees. It would be inefficient to spend time calculating the exact amount of attorneys' fees owed if the appellate court concludes that defendants are not contractually obliged to reimburse plaintiffs for their attorneys' fees. *See* Fed. R. Civ. P. 58 (Advisory Committee Notes, 1993 Amendments) ("Particularly if the claim for fees involves substantial issues or is likely to be affected by the appellate decision, the district court may prefer to defer consideration of the claim for fees until after the appeal is resolved."). Nothing

prevents the parties from appealing this Court's decisions regarding the merits of their claims at this time. *See Budinich v. Becton Dickinson & Co.*, 486 U.S. 196, 202 (1988) ("[A]n unresolved issue of attorney's fees for the litigation in question does not prevent judgment on the merits from being final."); *Farkas v. Rumore*, 101 F.3d 20, 22 (2d Cir. 1996) (*per curiam*) ("[W]here an order disposes of a party's substantive claims, but does not dispose of claims relating to attorney's fees, the time for appeal of the substantive claims starts to run from the date of the first order unless the district court explicitly grants a delay.") (citation to *Budinich* omitted). Accordingly, the amount of attorneys' fees and expenses to which plaintiffs are entitled will not be determined prior to any appeal.

Conclusion

Plaintiffs have failed to show by clear and convincing evidence that defendants are liable for constructive fraud, negligent misrepresentation and fraudulent omission. Additionally, I find that plaintiffs are collaterally estopped from bringing these claims. Accordingly, it is hereby

ORDERED, DECREED and ADJUDGED that judgment be entered for defendants.

SO ORDERED:

Shira A. Scheindlin
U.S.D.J.

Dated: New York, New York
February 10, 1997

APPENDIX D — EXCERPTS FROM EMPLOYEE RETIREMENT PLAN OF CLUETT, PEABODY & CO., INC. (AS AMENDED THROUGH JANUARY 1, 1985)

EMPLOYEE RETIREMENT PLAN

of

CLUETT, PEABODY & CO., INC.

(As Amended Through January 1, 1985)

(excerpts)

* * *

1.3 "Actuarial Equivalent" means an amount of equal value when computed on the basis of interest, mortality and other tables as shall be adopted from time to time by the Committee on the advice of the Actuary, the current factors being as specified below:

1. *Mortality table* The 1978 GAM Table (which is the 1971 Group Annuity Mortality Table projected to 1978 with Scale E). An average of male and female rates will be used.

2. *Interest rate* 5% per annum, compounded annually.

3. *Other factors* None.

* * *

Appendix D

9.6 Authority and duties of the Committee:

The Committee shall from time to time establish rules for the administration of the Plan and the transaction of its business. Except as herein otherwise expressly provided, the Committee shall have the exclusive right to interpret the Plan and to decide any matters arising thereunder in connection with the administration of the Plan. It shall endeavor to act by general rules so as not to discriminate in favor of any person. Its decisions and the records of the Committee shall be conclusive and binding upon the Company, Participants, and all other persons having any interest under the Plan.

The Committee shall adopt from time to time actuarial tables to be used as the basis for all actuarial calculations and shall determine from time to time the percentum rate or rates of interest to be used as the basis for calculations required in connection with the Plan. As an aid to the Committee, the Actuary appointed by the Committee shall make annual actuarial valuations of the assets and liabilities of the Plan and shall certify to the Committee the tables and rate or rates of interest which he would recommend for use by the Committee. The Committee shall receive and review the periodic valuation of the Plan made by the Actuary.

* * *

Appendix D

9.8 Appeals:

The Plan managers shall make all determinations as to the right of any person to a benefit. Any denial by a Plan Manager of a claim for benefits under the Plan by a Participant or a Beneficiary shall be stated in writing by the Plan Manager and delivered or mailed to the Participant or Beneficiary; and such notice shall set forth the specific reasons for the denial, written to the best of his ability in a manner that may be understood without legal or actuarial counsel. In addition the Plan Manager shall afford a reasonable opportunity to any Participant or Beneficiary whose claim for benefits has been denied for a review of the decision denying the claim. Such a Participant or Beneficiary shall have the right within 60 days of such decisions to appeal such decision to the Committee. A decision by the Committee shall be final and binding on all parties concerned.

APPENDIX E — EXCERPTS FROM AMENDED AND RESTATED DEFERRED COMPENSATION AGREEMENT

AMENDED AND RESTATED
DEFERRED COMPENSATION AGREEMENT (excerpts)

AMENDMENT AND RESTATEMENT made as of the 1st day of March 1984, of the DEFERRED COMPENSATION AGREEMENT made as of the 1st day of July, 1976 (as amended and supplemented), by and between CLUETT, PEABODY & CO., INC., a corporation with its principal place of business at 510 Fifth Avenue, New York, New York 10036, and Robert D. Krumme, residing at 98 Larchmont Avenue, Larchmont, NY 10538 (the "Executive").

. . .

Deferred Compensation means the payments to be made to the Executive pursuant to this Agreement following the termination of the Period of Employment.

. . .

9. The rights of the Executive to the Deferred Compensation and of the Beneficiary to the Contingent Deferred Compensation shall be solely those of unsecured creditors of Cluett. No assets acquired or held by Cluett, whether or not in connection with the obligations assumed by it hereunder, shall be deemed to be held under any trust for the benefit of the Executive or the Beneficiary or to be security for the performance of the obligations of Cluett, but shall be and remain a general, unpledged and unrestricted assets of Cluett.

APPENDIX F — EXCERPTS FROM AMENDMENT TO DEFERRED COMPENSATION AGREEMENT

AMENDMENT TO DEFERRED COMPENSATION AGREEMENT (excerpts)

This AMENDMENT made as of the 11th day of November, 1988 of the AMENDED AND RESTATED DEFERRED COMPENSATION AGREEMENT (the "Deferred Compensation Agreement") made as of the 1st day of March, 1984, by and between CLUETT, PEABODY & CO., INC. ("Cluett") and Robert D. Krumme (the "Executive");

. . .

4A.

(1) (c) The term "Actuarial Equivalent" means, with respect to an Accrued Benefit, and Deferred Compensation (or Contingent Deferred Compensation, as the case may be) benefit provided under the terms of this Agreement which has the same present value as the Accrued Benefit. For the purpose of establishing whether a benefit is the Actuarial Equivalent of another benefit the actuarial assumptions contained in Cluett's Employee Retirement Plan shall be employed for so long as that Plan remains in existence and if such Plan is no longer in existence, the actuarial assumptions last used by such Plan shall be used.

. . .

(2) Notwithstanding any other provision of this Agreement, upon the occurrence of a Change in Control the Executive (or the Executive's Beneficiary if the Beneficiary is then receiving Contingent Deferred Compensation payments)

shall be paid in a lump sum a benefit equal to the Actuarial Equivalent of the Executive's (or such Beneficiary's) Accrued Benefit as of the Change in Control Date, provided that the Executive's (or such Beneficiary's) rights to payments hereunder shall not have been forfeited under the provisions of Section 6 or Section 7 hereof, such lump sum payment to be made within 60 days of the Change in Control Date.

. . .

16. If at any time upon or after a Change of Control there should arise any dispute as to the validity, interpretation or application of any term of condition of this Agreement, or any Internal Revenue Service determination that the benefits under the Agreement constitute 'excess parachute payments' within the meaning of Section 280G(b) of the Code, subject to an excise tax under Code Section 4999, Cluett agrees, upon written demand by an Executive, to provide sums sufficient to pay on a current basis (either directly or by reimbursing the Executive or his legal representative) the Executive' costs and reasonable attorneys' fees (including expenses of investigation and disbursements for fees (including expenses of investigation and disbursements for the fees and expenses of experts, etc.) (a) incurred by the Executive in connection with any dispute or litigation, regardless of whether the Executive is the prevailing party, involving any provision of this Agreement, provided that the court in which such litigation is pursued determines, upon application of any party, that the Executive or his legal representative did not initiate frivolously such litigation, or (b) incurred by the Executive in connection with any Internal Revenue Service challenge concerning the status of benefits paid hereunder as 'excess parachute payments' subject to an excise tax. Under no circumstances shall the Executive or his

legal representative be obligated to pay or reimburse Cluett for any attorney's fees, costs or expenses incurred by Cluett. The provisions of this Section shall survive the expiration or termination of this Agreement and of the Executive's employment.

APPENDIX G — LETTER DATED FEBRUARY 16, 1989 FROM STEVEN A. HARROLD OF THE ACTUARIAL FIRM TPF&C TO BARRY F. SHEA, TREASURER OF WEST POINT - PEPPERELL, INC.

[Letterhead of TPF&C]

February 16, 1989

Mr. Barry F. Shea
Treasurer
West Point Pepperell
Post Office Box 71
West Point, Georgia 31833

Dear Barry:

One of our assignments, as Actuary to the Cluett, Peabody & Co., Inc. Retirement Plan, is to recommend to the Management Pension Committee the actuarial equivalence bases needed from time to time to convert one form of annuity benefit to another such form, or to a lump sum amount. This letter provides our recommendation for converting certain monthly annuities to lump sum amounts.

Section 13.2 of the Cluett plan provides for the conversion of monthly annuities of $100 per month or less to lump sum amounts. The document does not, however, provide for the payment of lump sum amounts if the monthly annuity is more than $100 a month. It is our recommendation that the actuarial equivalence basis used in the two West Point Pepperell qualified plans for lump sum payments be adopted for the Cluett plan. This actuarial equivalence basis is the one adopted for use in calculating amounts for lump sum payments under the recent Retirement Enhancement Program for participants in the Cluett plan.

Appendix G

The West Point Pepperell actuarial equivalence basis uses a "current" interest rate to convert monthly annuities to lump sum amounts. Before 1984, the West Point Pepperell plans used the greater of the Moody's AAA Bond Index and 10% for the interest rate. Now, the rate is defined as 120% of the PBGC immediate interest rate, unless the lump sum amount is less than $25,000. In the latter case, the lump sum is recalculated using the PBGC immediate interest rate, but the resulting lump sum is not permitted to exceed $25,000. The PBGC immediate rate during February 1989 is 7-¾%; 120% of that rate is 9.30%.

The Mortality basis used for the lump sum factors in the West Point Pepperell plans is one derived especially for West Point Pepperell by TPF&C, and is intended to be representative of West Point Pepperell's expected future mortality experience.

If you have any questions about this recommendation or would like to discuss this matter in more detail, please contact me.

Sincerely yours,

Steven A. Harrold

APPENDIX H — MINUTES OF FEBRUARY 16, 1989 MEETING OF WEST POINT-PEPPERELL, INC. MANAGEMENT PENSION COMMITTEE, ACTING AS THE COMMITTEE FOR THE CLUETT EMPLOYEE RETIREMENT PLAN

MEETING OF WEST POINT PEPPERELL MANAGEMENT PENSION COMMITTEE

On February 16, 1989, a meeting of the Management Pension Committee of West Point-Pepperell, Inc., was held at the Company's offices at the McGraw-Hill Building in New York City. Present were Messrs. J. L. Lanier, Jr., Clayton S. Sauers, C. Powers Dorsett and Barry F. Shea, constituting a quorum of the Committee. Mr. Dorsett acted as secretary for the Committee.

The purpose of the meeting was to consider the recommendation of TPF&C set forth in the letter dated February 16, 1989, addressed to Mr. Shea from Steven A. Harrell of TPF&C, a copy of which is attached to these minutes. After discussion of TPF&C's recommendation that the Cluett, Peabody & Co., Inc. Retirement Plan use the actuarial equivalence basis used in the West Point Pepperell qualified plans for lump sum payments, it was the unanimous decision of the Committee acting as the retirement committee under the Cluett, Peabody & Co., Inc. retirement plan to adopt TPF&Cs recommendation for such purposes.

There being no further business to come before the meeting, it was adjourned.

APPENDIX I — DEFERRED COMPENSATION AGREEMENT ELECTION FORM

DEFERRED COMPENSATION AGREEMENT ELECTION FORM

CHECK APPROPRIATE BOX

[ ] I understand that, as a result of the amendment dated November 11, 1988, to the Deferred Compensation Agreement between Cluett, Peabody & Co., Inc., and me, in the event of a change in control of West Point-Pepperell, Inc., I am entitled to receive in a lump sum payment the actuarial equivalent of my deferred compensation benefit under the Agreement. I understand that this lump sum will be calculated using a discount rate equal to 120% of the then current PBGC immediate interest rate, unless the lump sum amount is less than $25,000. If the lump sum amount is less than $25,000 using the above rate, the lump sum is to be recalculated using the PBGC immediate annuity rate, but the resulting lump sum is not to exceed $25,000. **I elect to have my deferred compensation benefit paid as a lump sum in the event of a change in control.** I understand that the lump sum payment of the actuarial equivalent of my deferred compensation benefit will be in full satisfaction of all obligations of West Point-Pepperell, Inc., as successor to Cluett, Peabody & Co., Inc., under the terms of my Deferred Compensation Agreement, and that in accepting a lump sum payment I shall thereby release West Point-Pepperell, Inc., its Directors, officers, employees, and agents, and its successors and assigns, from all obligations under the Agreement.

Appendix I

[ ] I understand that, as a result of the amendment dated November 11, 1988, to the Deferred Compensation Agreement between Cluett, Peabody & Co., Inc., and me, in the event of a change in control of West Point-Pepperell, Inc., I am entitled to receive in a lump sum payment the actuarial equivalent of my deferred compensation benefit under the Agreement. **I elect to revoke the November 11, 1988, amendment so that I will defer** receipt of my deferred compensation benefit pursuant to the terms and conditions of **the Agreement in effect prior to the November 11, 1988, amendment.**

_____

Signature

_____

Date

APPENDIX J — EXCERPTS FROM TRANSCRIPT OF DEPOSITION OF STEVEN A. HARROLD ON JULY 27, 1989

Deposition of STEVEN A. HARROLD, a non-party witness, taken by Plaintiff, pursuant to Subpoena, on July 27, 1989 (excerpts).

Q. And have there been persons who have left the company after February 16th, who received lump sum benefits?

A. Yes, sir.

Q. And have those people been paid out in lump sum under the $3,500 limit, using a five percent interest assumption or a 9.3 percent interest assumption?

A. A blend.

Q. A blend?

A. Yes.

Q. Would you please explain what you mean by a blend?

A. Sure. The benefits under the rules imposed by Congress and the Internal Revenue Service on qualified pension plans, the amount of the benefit earned up through a change date cannot be taken away from an individual.

The particular name given to what can't be taken away is an accrued benefit. So if you were to have a benefit that says you get $100 a month, if you have earned that through February 16th, the company can't change the formular such as that $100 a month is reduced.

Appendix J

Q. If they can't change the formular —

MR. TISMAN: I don't believe the witness is done.

A. The company could change the formular so that your benefit would have been $50 a month, but since you had already earned it before the formular was changed, that extra $50 is grandfathered for you.

Recent legislation has said not only is the amount of the benefit grandfathered for you, but some other attributes of the plan are also grandfathered.

For example these early retirement factors. As long as the benefits have been earned. So the fact is the lump sum actuarial equivalent basis grandfathered.

So the benefit earned up to February 16, 1989, under the qualified plan, will attract an interest rate of five percent. The amount of the benefit earned after February 16th will attract a benefit of 9.3 percent. I'm sorry not attract an interest rate of 9.3, it will attract an interest rate according to the West Point market rate factors.